Nos. 226, 227, 243, 266

IN THE

Supreme Court of the United States

OCTOBER TERM, 1948

Nos. 226, 227, 243

SECURITIES AND EXCHANGE COMMISSION, THOMAS W. STREETER, et al., THE HOME INSURANCE COMPANY, et al.,
Petitioners,

v.

CENTRAL-ILLINOIS SECURITIES CORPORATION, et al.

No. 266

CENTRAL-ILLINOIS SECURITIES CORPORATION and CHRISTIAN A. JOHNSON,
Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION, THOMAS W. STREETER, et al., THE HOME INSURANCE CO., et al.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF OF CENTRAL-ILLINOIS SECURITIES CORPORATION AND CHRISTIAN A. JOHNSON, RESPONDENTS-PETITIONERS

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Opinions Below

The opinion and judgment of the Court below (R. 12) and the opinion denying petitions and cross-petitions for

rehearings (R. 138) are reported at 168 F. 2d 722. The opinion of the District Court is reported at 71 F. Supp. 797 (R. 283a), but its detailed Findings of Fact and Conclusions of Law (R. 293a-317a) are not reported. The Findings and Opinions of the Securities and Exchange Commission dated December 4, 1946 and January 8, 1947, have not yet been officially reported, but are set forth in the Commission's Holding Company Act Releases Nos. 7041 (R. 25a) and 7119 (R. 128a).

Jurisdiction

The judgment of the Court of Appeals for the Third Circuit (R. 41) was entered March 19, 1948, and its order denying petitions and cross-petitions for rehearing (R. 140) was entered June 11, 1948. Petitions and cross petitions for writs of certiorari were filed on August 16 (Nos. 226 and 227), August 24 (No. 243) and September 8, 1948 (No. 266), and granted October 25, 1948. The jurisdiction of this Court is invoked under Section 240 of the Judicial Code as amended by the Acts of February 13, 1925, and June 25, 1948 (28 U. S. C. 1254), made applicable by Section 25 of the Public Utility Holding Company Act of 1935 ("the Act"), 49 Stat. 803 (15 U. S. C. Sec. 79a et seq.).

Statute Involved

The provisions of Section 11(e) of the Act, the statutory provision directly applicable here, are set forth in Appendix A, *infra*, pp. 159-165, together with the pertinent provisions of other sections of the Act referred to in this brief.

Questions Presented

1. Whether the "fair and equitable" standard contained in Section 11(e) of the Act authorized the Securities and Exchange Commission to award senior security holders premiums in contravention of applicable charter provisions and constitutional limitations, when under the compulsion of the Act the holding company enterprise was finally terminated and the senior security holders were paid out in cash.

2. Whether, assuming that the charter provisions were not applicable, the "fair and equitable" standard contained in Section 11(e) of the Act authorized such premiums in violation of settled legal principles repeatedly held applicable by the Commission and the Courts.

3. Whether, if the Act is found to authorize the payment to preferred stockholders, in appropriate circumstances, of sums representing the "equitable equivalent of rights surrendered", such "equitable equivalents" can be determined by appraising the "investment value" of the preferred stocks on the basis of transient market prices, and without regard to the correlative "investment value" of the common stock.

4. Whether the District Court was authorized under Section 11(e) of the Act to determine, and properly determined in this case, not only that the Securities and Exchange Commission erred in measuring the "equitable equivalents" which the preferred stockholders claim to be entitled to receive in exchange for the rights they surrendered, but that on any possible proper measure of those "equitable equivalents" on this record, $100 per share is the maximum to which the preferred stockholders are entitled.

Statement

Introductory

In essence, this litigation involves a dispute concerning the disposition of a fund of approximately $3,200,000 (plus $400,000 interest) paid into a bank in escrow by Engineers Public Service Company ("Engineers") pursuant to arrangements consummated during the proceedings before the United States District Court for the District of Delaware. The proceedings in the District Court related to a plan for the dissolution of Engineers pursuant to Section 11(e) of the Act, which dissolution has now been substantially carried out. The ultimate question at issue is whether this fund should be paid over to the former holders of the preferred stock of Engineers or should remain in the residual assets of the Company, to be distributed among the common stockholders. The Securities and Exchange Commission in effect held for the preferred stockholders; the District Court, while approving and enforcing the remainder of the plan, held for the common stockholders on this point. Upon appeal by the Commission and two groups of preferred stockholders,[1] the Court of Appeals for the Third

[1] In the District Court the Commission acts primarily as the statutory agent of the company in applying to such court for approval and enforcement of the company's plan, since Section 11(e) provides that the Commission may make such an application *only* upon the request of the company. The refusal of the company to appeal from the District Court's order therefore raised a question as to whether the Commission's statutory agency had not been revoked, and as to its right to assume the role of appellant. However, respondents advised the Court of Appeals that they did not press this question since they recognized that the issues were of importance in the administration of the Act and the Court would doubtless wish to be informed of the Commission's views.

Circuit agreed with the conclusion of the District Court that the disapproved portion of the plan was unfair and inequitable, but held that the proceedings should be remanded to the Commission. The appellants in the Court below petitioned for writs of certiorari with respect to the Court of Appeals' determination that the disapproved portion of the plan was unfair and inequitable, and this Court granted the writs (Nos. 226, 227, 243). Certain holders of common stock of Engineers who were appellees in the Court below (herein referred to as "Respondents") petitioned for a writ with respect to the Court of Appeals' requirement for the remand of the proceedings to the Commission, which petition the Court also granted (No. 266). This petition was supported by another group of common stockholders, sometimes referred to as the "Boehm-White Group".

Respondents Central-Illinois Securities Corporation and C. A. Johnson, on whose behalf this brief is submitted, are the owners of 5,000 and 1,000 shares of Engineers common stock, respectively.[1] They advised the Commission of their objections to the proposal to pay the preferred stockholders the amounts here in dispute as soon as the proposal was made (R. 2148a), and they appeared in the District Court and participated throughout the proceedings therein and the subsequent appeal, in their own behalf and in a representative capacity on behalf of all other common stockholders of Engineers (R. 153a).

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[1] Central-Illinois Securities Corporation, a Delaware corporation, is a publicly owned investment company registered under the Investment Company Act of 1940. It has 200,000 shares of preferred and 309,202 shares of common stock outstanding, owned by more than 2,100 stockholders residing throughout the United States.

The Plan and Necessity Therefor

The plan filed with the Commission by Engineers in September, 1945, was submitted in order to effect final compliance with a series of mandatory orders previously issued against Engineers by the Commission under Section 11(b) of the Act. These orders required Engineers to divest itself of one after another of its subsidiaries until only one, Virginia Electric and Power Company, should remain.[1] In addition, Engineers was formally warned by the Commission that unless it filed a "comprehensive plan" for complete compliance with these Section 11(b)(1) orders as well as for "readjusting its capital structure" to conform with the standards of Section 11(b)(2), it faced the likelihood of mandatory enforcement action by the Commission under Section 11(d) of the Act.[2]

The cumulative net effect of these Section 11(b)(1) orders, when taken in combination with the provisions of Section 11(b)(2) as interpreted by the Commission in

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[1] These orders are reported in the published decisions of the Commission as follows: *Engineers Public Service Co.*, 9 S. E. C. 764 (1941); 10 S. E. C. 904 (1941); 12 S. E. C. 41, 268 (1942). The United States Court of Appeals for the District of Columbia, on Engineers' petition for review, in part affirmed and in part reversed certain of the Commission's orders (*Engineers Public Service Co.* v. *S. E. C.*, 138 F. 2d 936 [App. D. C. 1943]). This Court in 1944 granted certiorari (322 U. S. 723, 1944), but the death of Chief Justice Stone apparently left the Court without a quorum and unable to issue a decision. The case was dismissed as moot by order of this Court (332 U. S. 788) pursuant to stipulation and joint motion of counsel entered into following entry of the decree of the District Court in the instant case approving and enforcing Engineers' plan, except as to the premium payments.

[2] *The Western Public Service Company et al.*, 12 S. E. C. 804, 808 (Feb. 15, 1943).

a series of decisions upheld by the Courts, was to require the complete and final dissolution of Engineers and its entire holding company system.[1] The plan submitted by Engineers accordingly proposed that Engineers and the remaining portion of its system would be wholly liquidated and dissolved.

As of the time the plan was submitted, the Engineers' system had been reduced to only three operating companies in the course of Engineers' compliance with various of the Commission's divestment orders, as compared with the 17 electric, gas and other utility and non-utility companies which had comprised Engineers' system at the time of the enactment of the Public Utility Holding Company Act.[2] The three remaining subsidiaries were Virginia Electric and Power Company ("Virginia"), Gulf States Utilities Company ("Gulf States") and El Paso Electric Company ("El Paso"), in all of which Engineers owned merely the common stock.[3] The Commis-

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[1] Engineers as a holding company having only a single subsidiary would be devoid of economic and functional utility—or, in the Commission's parlance, "an economic monstrosity" (R. 47a). The Commission has repeatedly held that such a holding company is offensive to the standards of Section 11(b)(2), and must be dissolved. See, *National Power & Light Co.*, 9 S. E. C. 978; *North American Light & Power Co.*, 10 S. E. C. 924, discussed in *City National Bank and Trust Co. of Chicago* v. *S. E. C.*, 134 F. 2d 65 (C. C. A. 7); *Standard Power & Light Corp.*, 11 S. E. C. 689; *American Power & Light Company*, 11 S. E. C. 1146, aff'd 141 F. 2d 606 (C. C. A. 1st) and 329 U. S. 90. Cf. *Northern New England Company*, Holding Company Act Release No. 8401 (1948) at p. 6.

[2] Engineers Ex. No. 37-C, p. 67, R. 1478a. Of these seventeen companies, nine were direct subsidiaries of Engineers, and eight were indirect subsidiaries.

[3] The common stocks of these operating companies represented only 20-30% of the total capitalization of each company. All three companies have large amounts of bonds and preferred stocks outstanding with the general public.

sion's outstanding Section 11(b)(1) orders expressly required divestment of the stocks of both Gulf States and El Paso.

Engineers' capital structure consisted of common stock and preferred stock, the latter all having a stated book value of $100 per share (increased in 1938 from $96 per share, R. 301a) but being divided into three series carrying different dividend rates ($5, $5.50 and $6), and all being entitled in the event of liquidation, dissolution, winding up or any "reduction of its capital stock, resulting in any distribution of its assets to its stockholders" to $100 per share plus accrued dividends in preference to any payments to the holders of the common stock. However, if such liquidating acts were "voluntary", the preferred holders would, in addition, be entitled to the redemption premiums of each series (i.e., $5 per share for the $5 series, and $10 for the others). Under the provisions of the charter, the preferred stocks were callable at any time at the option of the company upon payment of these redemption amounts, and the company had the right at any time to repurchase shares of its preferred stock at prices "not exceeding" the redemption prices.[1]

Engineers' plan, so far as here material, provided in substance: (1) that the common stockholders of Engineers should initially pay $22,000,000 in cash into Engi-

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[1] The pertinent provisions of the charter (Engineers Ex. 33, R. 1403a *et seq.*) are set forth in Appendix B, *infra*, pp. 166-7. It is to be observed that the charter expressly provided that in the event of liquidation, dissolution, winding up, etc., upon payment of the amounts stated above, the holders of the preferred stock "shall be entitled to no further participation in such distribution", and that the holders of the the common stock "shall be entitled to receive, *pro rata*, all of the remaining assets of this corporation available for distribution to its stockholders" after paying or making provision for the aforesaid amounts payable to the holders of the preferred stock.

neers' treasury;[1] (2) that this money plus treasury cash on hand (representing the proceeds of other property sales and retained earnings), supplemented by a short-term bank loan, would be used to effect the retirement of all the preferred stock of Engineers at $100 per share, plus dividends to the date of payment; (3) that promptly thereafter, the common stocks of El Paso and Virginia would be distributed among the 13,000 common stockholders of Engineers[2] as a final liquidating dividend; and thereupon Engineers, as well as the system's service company "Epsco", would be dissolved.

Commission Decision

In its Findings and Opinion issued December 5, 1946, the Commission found that the dissolution of Engineers was an involuntary dissolution made necessary by the mandatory provisions of Section 11 of the Act stating:

> "We find that the presence of Engineers would unduly complicate the structure of the system and

[1] This was to be accomplished by the issuance to the common stockholders of warrants entitling such stockholders to purchase one share of Gulf States common stock at $11.50 per share, for each share of Engineers common owned. In effect, therefore, this constituted a special assessment on the common stockholders for the privilege of receiving one of their company's assets in liquidation. If the stockholder did not exercise the warrant he would forfeit his *pro rata* share of the Gulf States stock thus distributed. He might, however, realize a small amount if he sold the warrant.

[2] There are 1,999,968 shares of Engineers common stock outstanding, of which the largest single holder of record owns approximately 99,643 shares (Engineers Ex. 43; R. 1769a). The record establishes that this block of stock is actually beneficially owned by a substantial number of separate individual owners (R. 561a-570a). It may further be noted that this same record stockholder was also among the largest owners of all three series of preferred stocks (Engineers Exs. 40, 41, 42, R. 1762a, 1763a, 1767a).

that it would, therefore, come within the prohibition of Section 11(b)(2). Accordingly, we find that the proposal to dissolve Engineers is 'necessary' to effectuate the provisions of Section 11(b) of the Act" (R. 48a).

The Commission further found that the Act required the dissolution to be carried out forthwith, and disapproved one feature of the plan which would tend to delay somewhat the final step in liquidation.[1]

Despite its finding that the dissolution of Engineers and its system was not voluntary, the Commission held that the company must pay the preferred stockholders the redemption premiums which the charter provided were payable only in the event of a voluntary liquidation or redemption. The Commission refused to approve the plan until the company amended it to provide for the payment of such premiums (R. 84a-85a). These premiums totalled $3,204,795 in excess of the amounts specified by the charter as payable to the preferred holders in the event of liquidation, dissolution, winding-up or "reduction of * * * [the corporation's] capital stock, resulting in any distribution of its assets to its stockholders."

In reaching this result, which was directly contrary to a long line of Commission and Court decisions,[2] the Commission's initial postulate was that *Otis & Co. v. S. E. C.*, 323 U. S. 624, established the proposition that

[1] "We have found that the continued existence of Engineers would unduly complicate the system. The Act requires that unnecessary entities be eliminated 'as soon as practicable'. Under these circumstances, the desire of stockholders to withhold income and thereby realize capital gains cannot justify ignoring the plain dictates of the Act" (R. 59a).

[2] See p. 55, note 3, *infra*.

charter liquidation provisions were not controlling in any liquidations under the Holding Company Act, but were merely one factor to be taken into account (R. 61a-62a). It thereupon disregarded these charter provisions entirely.

The amount which the preferred stockholders must receive, the Commission held, was "the investment value of their stock on a going-concern basis", and as though no liquidation were taking place (R. 67a-68a). The Commission noted that two witnesses (Badger, a witness on behalf of certain preferred holders, and Barnes, president of Engineers) had testified that on a "going-concern basis" and "if there were no Holding Company Act, or if the Act were to be repealed today" (R. 67a) they believed Engineers' preferred stocks would sell on the market at or about their redemption prices and would probably be called and redeemed by the company.[1] The Commission thereupon stated that it was "apparent", and "not seriously challenged", that "the preferred has an investment value at least equal to the respective redemption prices"; and it held that this was the amount they must be paid (R. 67a-68a).

No mention was made by the Commission of Barnes' repeated and emphatic testimony that such "values" largely reflected the inflated stock market prices current

[1] Barnes, one of the two witnesses referred to, pointed out that "if there were no Holding Company Act, or if the Act were to be repealed today" so that Engineers were not compelled to liquidate, it would, of course, take advantage of the current low money rates to replace its outstanding preferred stock with preferred stock carrying a much lower dividend rate, thereby benefiting the common stockholders substantially (R. 522a, 663a). The Commission's opinion made no reference to this portion of Barnes' testimony.

at that moment,[1] and could by no means be deemed the "fair value" of the stock for any representative period of time in the light of its poor past record and future uncertainties (R. 522a-526a; 1138a-1146a). Despite the fact that the amounts to which the Commission held the Engineers' preferreds entitled were admittedly the maximum which could be awarded if the stock were the highest grade of "gilt-edge" security, no mention was made by the Commission of Badger's admission that the Engineers' preferreds were not "high grade" but at best "medium grade" (R. 1133a. 1185a); nor of Barnes' testimony that on the basis of the criteria customarily employed by financial analysts they are "closer to a low-grade preferred" (R. 1133a., 1140a); nor of the evidence establishing that during the period the preferreds were outstanding they were accorded by the leading independent analysts an investment rating of only C**.

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[1] The testimony of Badger and Barnes was given at various times over the period December 1945 through February 1946, at which time stock market prices (including those of public utilities) stood at the highest point since 1931. Barnes warned "we are in a boom period" (R. 667a) and stressed its temporary nature. The Federal Reserve Bank Index of utility stock prices which stood at 130 in June 1946 subsequently declined to 94 by the end of 1947, indicating an average decline of about 28% (cf. Federal Reserve Bulletins: January 1947, p. 64; January 1948, p. 76).

In a more recent decision, the Commission itself stated concerning "investment values" determined as of this very period:

> "* * * the Commission's findings were issued in May of 1946 *in what has since proven to be the peak of the post-war market.* The market has declined substantially from the highs reached at that time and there has been a material firming of interest and preferred yields. It is apparent that insofar as investment value is derived from an analysis of the current yields of comparable securities, *the investment value of American's preferred has been substantially affected in the interim*" (*United Light and Railways Co.-American Light & Traction Co.*, Holding Company Act Release No. 7951, p. 33, Dec. 31, 1947; emphasis supplied).

defined as "Preferred stocks with erratic dividend records which can be expected to make payments only under favorable conditions" (R. 1844a-1845a).[1]

Although the Commission purported to be determining the "investment value" of the preferred stock on a going-concern basis", and "as though no liquidation were taking place", in fact its valuation technique departed sharply from accepted methods of valuation in reorganization proceedings and from that approved by this Court in *Otis v. S. E. C.*, 323 U. S. 624. The Commission made no effort to appraise the value of Engineers' stock, either preferred or common, in long range terms. It did not even attempt the characteristic estimate of the prospective earning power of the system[2] in an effort to establish what each class of security holders was losing by the liquidation of the company. It sought merely to de-

[1] In an earlier portion of its opinion, the Commission did summarize statistically evidence in the record establishing that the preferred stocks had been in arrears of dividends for several years and had sold for considerable periods of time as low as \$10-\$14 per share for all series, and that the overall market price through the entire period from the time of issuance to the date of the testimony was only \$63-\$67 per share for all series (R. 62a); but no reference was made to these factors at the point where the Commission discussed the so-called "investment values".

Similarly, although the Commission's computations showed that these preferreds were actually a speculative *junior security* (being junior to 66.2% of the system's capitalization, R. 64a), no allusion to the significance of this factor is to be found anywhere in the opinion; nor is allusion made to the significance of the slim coverage for charges and dividends over the past decade (R. 64a) nor of the fact that for several years continuously charges and dividends had not been fully earned.

These omissions are particularly noteworthy in view of the fact that in the long line of decisions in which the Commission theretofore had refused to approve payment of premiums upon retirement of senior securities, it had repeatedly stressed all of these very factors. (See decisions cited, p. 55, notes 3 and 4, *infra*.)

[2] Cf. *Consolidated Rock Products Co. v. DuBois*, 312 U. S. 510, 526; *Group of Institutional Investors v. Milwaukee R. Co.*, 318 U. S. 523, 565-6.

termine how much should be paid to the preferred stockholders as the "equitable equivalent" of their rights on a "going concern basis", and "apart from the impact of the Act", viewing the preferreds' rights as though they were something absolute, and unrelated to the correlative rights which the common stockholders would have in such a "going-concern".

Moreover, in evaluating the "rights" of the preferred stockholders on this unilateral basis, the Commission merely accepted Badger's estimate of the hypothetical market prices at which the preferred stocks would have sold at the time of his testimony, assuming liquidation were not to take place. But Badger's "expert opinion" as to the theoretical market price of the Engineers' preferred stocks "apart from the impact of the Act", which the Commission adopted, was not based on the intrinsic merit of this stock as an investment, but admittedly upon the unprecedentedly low *money rates* then prevailing. Because of these low money rates Badger contended that Engineer's high dividend preferred stocks would have an enhanced market value, if the Act did not compel their retirement.[1] The Commission's opinion accorded no con-

[1] With respect to the then prevailing money rates (which he employed without modification in "valuing" the Engineers' preferreds) Badger testified " * * * yields on preferred stocks are at the present time the lowest which they have been in the history of our country, or, conversely * * * the prices of such stocks are at the highest levels ever experienced. The permanency of this situation will depend on the permanency of low interest rates" (R. 2065a). Not only did Badger repeatedly and emphatically affirm the "permanence" of these unprecedentedly low money rates on which he predicated the "values" of the Engineers' preferreds (R. 2066a, 1019a, 1085a), *but the only possibility of change which he envisaged was the likelihood of money rates and yields going even lower* (R. 1085a-1086a). Several months from the time this testimony was given money rates and preferred stock yields commenced the sharp upward climb, and preferred stock prices the concomitant decline, which has been in progress ever since (see District Court Finding No. 52; R. 314a, and R. 122, as well as the Commission's own admission quoted *supra*, p. 12, n. 1).

sideration to the instability of those money rates, or to the question of other future developments which might affect the "value" of the preferred stocks, notwithstanding the contentions of the company and Barnes concerning the essentially artificial and transient character of the then current money rates and the various other potentially adverse factors to be taken into account in determining the actual value of those stocks on a "going concern basis".

Further, while allegedly determining values "ex the Act" (apart from the impact of liquidation compelled by the Act), neither the Commission nor Badger made allowance for the many important factors which came into existence directly as the result of this very statutory requirement for liquidation.[1] None of the other drastic impacts of the Act upon the common stockholders received consideration; nor did the Commission attempt to "find" the so-called "investment value" or any other value of the common stock on "a going-concern basis" (apart from the necessity for liquidation) or otherwise.

The District Court's Decision

After consideration of extensive oral argument and briefs by counsel for the Commission and all the other parties, the District Court (to which the Commission had applied pursuant to Section 11(e) for entry of a

[1] For example, no allowance was made for approximately $24,000,000 which had accrued to the equity of the common stockholders of Engineers and which had been withheld from them largely because of the necessity of providing *for this very liquidation* imposed upon them by the Act (R. 306a, 468a-471a; 578a; Engineers Ex. 30, R. 1395a). Instead this entire amount (equivalent to 60% of the preferreds' stated value) was credited to the preferred in determining its so-called "investment value *ex* the Act" (R. 306a, 312a).

decree approving and enforcing the plan) held that the provision of the amended plan for the payment of the amounts in excess of $100 per share (the premiums)[1] was not consonant with the "fair and equitable" standard of Section 11(e), but that in all other respects the plan met the statutory requirements. The Court thereupon followed the course strongly urged by the Commission's attorneys,[2] of not remanding the proceedings to the Commission, but instead, of approving and enforcing the plan except as to the premium payments, and requiring the latter to be deposited in an escrow fund approved by the Commission pending review of the District Court's determination. The Commission's opinions had expressly advocated this course (R. 75a, 136a), and its order of February 11, 1948 (R. 165a), had provided formal advance approval for it.

The disagreement of the District Court with the Commission as to the premium payments was basically a disagreement as to applicable legal principles. The Court regarded as erroneous and devoid of judicial support the Commission's thesis that the rights of security holders of a holding company enterprise which is being entirely and definitively liquidated pursuant to governmental edict should be approached on the purely fictional hypothesis that "the enterprise continues", and the claims of the preferred holders (but not the common) measured "on a going-concern basis", and "as though there were no Holding Company Act or as if the Act were to be repealed

[1] Following the issuance of the Commission's opinion of December 4, 1946, refusing to approve Engineers' plan unless amended to provide for payment of the premiums, the company duly amended its plan in the manner required by the Commission (R. 128a).

[2] R. 257a-261a, 281a-282a.

today" (R. 292a, 311a, 315a-316a).[1] The District Court was of the view that this recently evolved "investment value ex the Act" doctrine, as sought to be applied by the Commission in the case at bar, contravened firmly rooted decisions of at least four circuit courts of appeal and many district courts, as well as a long line of decisions of the Commission itself (R. 288a, 292a).[2]

Upon examination of the record which had been filed by the Commission with the Court, the District Judge ascertained a number of factors of which the Commission's opinion gave little or no inkling and which he found strongly corroborative of his view that payment of the premiums to the preferred would result in unfairness and inequity in a "colloquial" sense, as well as in its technical statutory sense; that Badger's "values" were largely "market" values (R. 301a) admittedly dependent upon

[1] It may be noted that the District Judge (Judge Leahy) had been the first court to pass upon and approve the United Light plan subsequently upheld by this Court in *Otis & Co. v. S. E. C.*, 323 U. S. 624, the decision relied upon in the instant case by the Commission as support for the proposition here rejected by the District Court. Judge Leahy's cogent understanding of the issues involved in the *Otis* case is attested by his decision therein (51 F. Supp. 217; D. Del., 1943). Similarly, Judge Biggs, who wrote the Court of Appeals' opinion in the instant case, was also the author of that Court's opinion in the *Otis* case (*In re Securities and Exchange Commission* [*Otis & Co.*], 142 F. 2d 411, C. C. A. 3, 1944).

[2] Decisions cited at p. 55, notes 3 and 4, *infra*. Judge Leahy had himself repeatedly and uniformly upheld the Commission's determination that such premiums were not payable, although envisaging that a contrary view might possibly be justified upon proof of "a different fact situation" (*In re North Continent Utilities Corp.*, 54 F. Supp. 527, D. Del.). As the Court of Appeals had occasion to point out (R. 30, 39) Judge Leahy, commencing with the earliest enforcement cases under the Act and continuously ever since, has had exceptionally specialized experience with Section 11(e) reorganizations, the Commission having applied to him for approval and enforcement of almost 50% of all Section 11(e) plans which have been brought to the courts for enforcement.

continuance of governmental "pegging operations" designed to hold money rates to the artificially low level considered desirable because of the exigencies of governmental war financing (R. 313a-314a); that on the basis of the inherent investment qualities of the stocks, they were admittedly not "high grade" but rather "*medium* medium grade" or "low grade" (R. 311a); that even such inherent value as they possessed was in substantial part due to the more than $24,000,000 of earnings which the common stockholders had left in the enterprise to provide for the liquidation commanded by the Act (R. 306a); that the company had sustained heavy losses and sacrifices in carrying out the Commission's Section 11(b)(1) divestment orders, and that such losses had fallen, and further deprivations incident to the liquidation would necessarily fall, on the common stockholders (R. 307a-308a); that the common stockholders had gone without dividends or return of any kind for 15 years while the preferred stockholders received full payment of their dividends over the entire period, aggregating approximately $90 per share (R. 302a, 306a); that in order to pay the preferred holders their full liquidating claim in cash the common stockholders would be required in connection with the liquidation to contribute an additional $22,000,000 cash, and to "mortgage" the assets distributable in the liquidation by advance payment of dividends (R. 308a-310a); that the common stockholders like the preferred stockholders were forced to relinquish continuance of the holding company enterprise in which they had invested (R. 311a, 312a, 316a).

The Court summed up its conclusions by formally finding that the enterprise in which the preferred and common stockholders of Engineers had invested had been frus-

trated and terminated by governmental action (R. 316a); that there was no valid basis for hypothesizing a "continuing enterprise" or "going concern" (R. 292a, 316a); that the Commission's "investment value ex the Act" doctrine as applied in this case was not only unsound and unrealistic in theory but inequitable and erroneous in application (R. 292a, 316a-317a). It held in the light of its "careful examination of all the relevant factors" that payment to the holders of the preferred stocks of Engineers of any amounts in excess of $100 per share plus accrued dividends would not be warranted or justified; would be unfair and inequitable to the holders of Engineers' common stock; and would contravene the "fair and equitable" standard of Section 11(e) of the Act (R. 317a).[1]

The Decision of the Court of Appeals[2]

The Court of Appeals rejected the Commission's contention that the District Court under Section 11(e) should be deemed a mere review court which must bow to the Commission's conclusions unless they wholly lack "any

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[1] The District Judge stated that he found it unnecessary to conclude whether the charter liquidation provisions *per se* foreclosed any amounts in excess of $100 per share plus dividends, because "the conclusion is reached that the preferred stockholders are in any event not entitled to receive any such excess amounts on the basis of all the relevant considerations, even if the charter provision is not itself controlling. Said charter provision, however, if taken into account, constitutes an additional factor supporting the conclusions reached, as above stated" (R. 317a).

[2] Following the entry of the District Court's order, notice of appeal to the Third Circuit Court of Appeals was filed by the Commission and the two groups of preferred stockholders, one of which sought to stay consummation of any portion of the plan. The Commission joined in opposing the stay, which was denied in turn by the Dis-

rational or statutory foundation" (R. 21, 34),[1] and held, after careful analysis of the statute and its legislative history, that a Section 11(e) Court must exercise its independent judgment as to the fairness and equity of a plan (R. 23, 33). It found that the District Judge treated the Commission's findings "as was proper * * * with respect" (R. 34), and commended his "careful and far-reaching examination of the relevant factors" (R. 34). It held that the Commission, in failing to take these important factors into account, had reached an inequitable and erroneous result (R. 38).

With respect to the Commission's attempted reliance on the *Otis* decision, the Court of Appeals agreed with the District Court that the liquidation of the Engineers system was a complete and definitive termination of the enterprise, and thus differed materially from the mere simplification of a continuing holding company system involved in the *Otis* decisions (R. 36).[2] It held that even if it was permissible under these circumstances to measure security holders' rights on the fictional hypothesis of a "going concern" without regard to the liquidation which was in fact taking place under compulsion of the Act (i.e., "*ex*

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trict Court, the Circuit Court and by Mr. Justice Burton of this Court. Thereupon, the escrow fund was duly established and the other provisions of the plan were consummated, including payment to the preferred stockholders of $100 per share and accrued dividends.

[1] The Court pointed out that the Commission's demand that Section 11(e) courts should be relegated to the position of mere review courts was at sharp variance with the position which the Commission has for many years taken before the courts and before Congress, wherein the independent plenary role of the District Court with respect to 11(e) plans was heavily emphasized (R. 30-31).

[2] As was pointed out, *supra* (p. 17, n. 1), Judge Biggs wrote the Third Circuit's opinion in the *Otis* case as well as in the case at bar.

the Act"), the so-called "investment value" formula as applied by the Commission in this case to measure only the claims of the preferred holders "ex the Act" failed to produce that "equitable equivalence" for the rights of both classes of security holders which is of the very essence of the *Otis* rationale (R. 38).

The Court of Appeals squarely affirmed the determination of the District Court that the provision of the plan for the payment of the premiums was unfair and inequitable (R. 39, 140). It also found "proper" and upheld the escrow arrangements embodied in the District Court's order (R. 30). Yet, notwithstanding its full approval of the District Court's reasoning and findings, the Court of Appeals concluded that the District Court should have remanded the proceedings to the Commission.

On the question of remand, the Court's reasoning was, in essence, that the disapproval by the District Court of the provision for payment of the premiums effected an "amendment" of the plan which, under the statute, must receive the Commission's approval as well as of that of the Court (R. 39). In addition, the Court of Appeals' opinion suggests that the District Judge engaged in a species of "valuation" in formally finding that payment to the preferred holders of $100 per share plus dividends would be fair and equitable to the preferred and that payment of any additional amounts would contravene the "fair and equitable standard" of Section 11(e), instead of merely holding the premium payments as proposed in the plan unfair and inequitable and remanding the plan to the Commission. Stating that "The problem is and will remain until its disposition by the Commission, one of valuation of the securities of Engineers, viz., the pre-

ferreds and the common" (R: 40), the Court vacated the decree of the District Court[1] and remanded the proceedings to it:

> "with directions to enter an order disapproving the plan as not being fair and equitable within the purview of Section 11(e) of the Public Utility Holding Company Act, and to return the record to the Commission to the end that it may take such action as the facts and the law may require" (R. 40, 41).

Petitions for rehearing were filed by the appellants in the Court below with respect to the Court's affirmance of the determination that the proposed payment of the premiums was unfair and inequitable. Answers thereto and cross-petitions were filed by the appellees (including petitioners) with respect to the requirement for remand to the Commission (R. 97). The Court denied the petitions and cross-petitions, stating in a short opinion its adherence to the views previously enunciated (R. 138).

Specification of Errors

That the Court of Appeals erred:

1. In finding that the District Court, by requiring the premiums to be paid into an escrow fund, had "amended" the plan without the requisite approval of the Commission;

2. In finding that the District Court engaged in a prohibited species of valuation as the result of holding that "fairness and equity" interdicted payment to the

[1] It is clear that the Court intended to vacate only so much of the District Court's decree as related to the premium payments since the remainder of the plan had already been fully consummated.

preferred stockholders of any amounts in excess of $100 per share rather than merely holding that the plan was unfair and inequitable in proposing to pay the preferred stockholders amounts in excess of $100 per share;

3. In vacating the decree of the District Court instead of affirming it; and

4. In requiring that the proceedings be remanded by the District Court to the Securities and Exchange Commission.

Summary of Argument

I

The term "fair and equitable", as used in Section 11(e) of the Act, is a term of art with a well developed historical meaning. It commands enforcement of the contractual rights and limitations of the security holders. Although it permits transmutation of those rights into equitable equivalents when continuance of the enterprise in reorganized form renders literal compliance with the contract "impossible", it never authorizes aggrandizement of the rights of one class of security holders, or disregard of that class' limitations, for this would necessarily entail invasion of the rights of other classes.

Nothing either said or ruled by this Court in the *Otis* case alters the historical meaning of the term "fair and equitable" and its command for the observance of contract rights. In that case, it was held that the preferred stockholders were accorded their full contractual rights in the form of a carefully measured participation in the earnings of the continuing holding company enterprise.

They were found to have no contractual right to the "acceleration" or "maturing" of their full liquidation claim, since authentic liquidation within the contract contemplation was not occurring. But here the preferred stockholders have claimed, and were allowed by the Commission, $3,200,000 in excess of their full matured liquidation claim despite the fact that the liquidation of the enterprise and the retirement of the preferred stock was squarely within the purview of the charter contract.

Since the plan now being reviewed provided for a complete termination of the enterprise, both of the holding company and of its entire system, and a final distribution in liquidation of the assets to the security holders—as the Courts below found—and since the liquidation was compelled by the Act, and was therefore not "voluntary"—as both the Commission and the Courts below found—it comes squarely within the terms "liquidation, dissolution or winding up" of Engineers' charter as those terms are used in the provision limiting payment to preferred stockholders to $100 per share.

Not only was the liquidation of Engineers an authentic complete dissolution of the entire holding company enterprise as distinguished from the mere "simplification" of a continuing holding company system considered in the *Otis* case, but the Engineers' charter provisions were also significantly different from those involved in *Otis*.

The fact that the Act had not been adopted in 1925, when Engineers' charter was framed, does not detract from the conclusion that it is applicable to this liquidation. At that time legislation to dissolve public utility holding companies was in contemplation, and such proposals were widely known. The specific provision of the Engineers'

charter specifying payment of no more than $100 per share to preferred stockholders if their stock were retired pursuant to a "reduction of its capital stock, resulting in a distribution of its assets to its stockholders", plainly applies to a reduction stemming from the break-up of the "power trusts" contemplated by the Senate at that time.

II

Even if the charter liquidation provisions were deemed not to apply to the liquidation which here occurred, the "fair and equitable" standard embodied in Section 11(e) precludes payment to senior security holders whose securities are being retired by the payment of cash, under the compulsion on the statute, of more than the face amount of their claim. Not only is this the meaning of the term "fair and equitable" in Section 11(e), as construed by the Commission and enforced by the Courts in a long and deeply-rooted series of cases, but the rationale upon which the Commission and the Courts based this interpretation of the statute applies compellingly to the facts of this case.

III

If the "fair and equitable" standard is not construed either to require enforcement of contractual rights or to conform to the manifestly correct prior interpretation thereof given by the Commission and the Courts, pressing constitutional problems are presented. The Commission's claimed power to alter contract rights in this case is neither necessary nor appropriate to accomplish the legitimate congressional purpose in adopting this statute; and the resulting absence of any standards by which to measure the Commission's exercise of its claimed power to alter contractual rights would entail an unconstitutional delegation of power to the Commission.

IV

Assuming that, notwithstanding our previous contentions, the "fair and equitable" standard nevertheless authorized transmutation of the rights of the Engineers' stockholders on a "going-concern basis" into equitable equivalents as was done in *Otis*, the fact is that the determination made by the Commission failed by a wide measure to satisfy such requirements.

In the *Otis* decision the term "investment value" as employed by this Court had reference to the values on a long range basis of both classes of stockholders, predicated upon the relative rights of each class to participate in the prospective earnings of the enterprise. Here the Commission made no attempt to estimate the prospective earnings of the enterprise which it hypothesized as continuing. It accorded no consideration whatever to the correlative rights of both classes of security holders in the theoretical "going-concern". It confined itself to considering solely the "rights" of the preferred stockholders; and although purporting to consider them on a "going-concern" basis, in fact it viewed them as absolutes, wholly unrelated to the correlative rights which the common stockholders had in that going concern.

Moreover, in thus evaluating the "rights" of the preferred stockholders unilaterally, the Commission eschewed normal, long-range values and measured them solely on the basis of market prices of allegedly comparable preferred stocks, as of a specific haphazard moment. At that moment the prices of those preferred stocks avowedly stood "at the highest levels ever experienced". During the years immediately preceding they were sharply lower,

and during the period which has ensued since the valuation testimony was given they have once again dropped to substantially lower levels. They had already commenced their decline and were in the process of further revision before the District Court passed on the plan.

Both Courts below found that the Commission's "investment value ex the Act" doctrine as applied in the instant case utterly failed to produce that "equitable equivalence" for surrendered stockholders' rights which the *Otis* decision commands.

If the Commission had sought to evaluate the rights of the preferred stockholders on any normal long-range basis, whether considered in terms of the past, the future, or both, there was no possible basis for a finding in excess of $100 per share. Moreover, if the rights of both classes of stockholders had been determined on a going-concern basis as was done in *Otis*, it is indisputable that the preferred stockholders would be entitled to considerably less than $100 per share.

V

The "investment value *ex* the Act" doctrine as here applied by the Commission, involves a dangerous and fundamental perversion of the strict priority principle, which is firmly embedded in the "fair and equitable" standard of Section 11(e).

Applying that doctrine, the Commission held that the preferred stockholders must receive more than their contractual claim in liquidation because their dividend rates were somewhat higher than the then current going rate. It would follow that senior security holders must re-

ceive less than their contract preference if their dividend or interest rate at the date of liquidation is lower than the going rate, irrespective of the fact that more than enough assets are available to pay their contract claim in full. Thus, the holder of a $1,000 bond amply protected by assets but carrying an interest rate of 4% could be required to accept a cash payment of $800 in full satisfaction of his rights if the Commission found that bonds of allegedly comparable quality were at that time selling on a 5% yield basis.

Conversely, this same use of current market prices (for which the term "yield basis" is a synonym) to evaluate the rights of senior security holders when yields on senior securities are low, must necessarily have a drastic impact upon the junior security holders. If a holding company had outstanding (as some do) several issues of non-callable senior securities, a Commission order, requiring the common stockholders to pay to the senior security holders the theoretical market prices "apart from the impact of liquidation" and in disregard of prearranged contractual arrangements, might well leave little or nothing for common stocks having substantial values on both an asset and earning power basis.

VI

One of the major fallacies in the Commission's rationale is its implicit assumption that if the preferred stockholders sustained a deprivation by reason of the compulsory retirement of their preferred stock upon payment of $100 per share, the common stockholders necessarily became the beneficiaries of that deprivation. But as this Court has said, "frustration and appropriation are essentially different things."

Even if it were true that "if not for the necessity of liquidation" the market might momentarily have paid a premium for these preferred stocks because they carried dividend rates somewhat higher than the money rates current at the time of Badger's testimony, plainly the common stockholders did not gain these hypothetical premiums when the preferred was retired at par under the compulsion of the Act. Such "premiums" were exclusively a factor of money rates applicable to senior securities such as preferred stocks and bonds. The common stockholders did not receive those preferred stocks which they could reoffer on the market to realize the theoretical premiums. Nor were they or the company permitted to issue any other senior securities so that they might benefit from the retirement of the preferred stocks at a time when money rates were low. Instead, they were required to completely liquidate what remained of the company and the system. And in that dissolution they suffered serious deprivations and losses in addition to those previously sustained.

Indeed, the compulsory retirement of the preferred stock itself constituted a serious deprivation to the common. If not for the Act, the common stockholders would have been free to retain the capital of the preferred without any limitations of time at an overall cost of 5.40%, while realizing some 12% on this capital; or, in the alternative, the common stockholders had the option of calling the preferred stock and replacing it with preferred carrying a lower dividend rate.

This substantial deprivation constituted but one of the many which the common had been forced to bear in carrying out the statutory mandate to liquidate. That liquidation did not commence with the filing of the plan which

was the subject of these proceedings; it merely ended there. The common stockholders had borne the full brunt of the liquidation of the system during the preceding ten years, and had safeguarded the preferred from even the slightest loss or deprivation. The District Court's conclusion that it was not consistent with fairness and equity to require the common to now indemnify the preferred for the "theoretical loss of their disappointed *expectations*" is inescapable under this Court's ruling in *Otis* that "enforcement of an overriding public policy should not have its consequences visited on one class with a corresponding windfall to another".

VII

Even under the narrowest possible construction of the powers of the District Court under Section 11(e) of the Act—the construction contended for by the Commission but overruled by both Courts below—the District Court properly disapproved the plan, since the Commission's approval thereof lacked "rational and statutory foundation" and the Commission had "plainly abused its discretion".

But we submit that, in passing upon a plan presented to it for approval under Section 11(e), the District Court does not sit as a mere "review court" limited to determining whether the Commission's action lacked rational and statutory foundation or whether the Commission plainly abused its discretion. When asked to enter its decree approving and enforcing a plan as "fair and equitable", the District Court sits as a court of equity, clothed with all the powers traditionally exercised by a court of equity, and charged with the duty to decide for itself, independently of the Commission's decision, whether the plan is

fair and equitable. The findings and conclusions of the Commission are entitled to "respect", but they are "not binding" upon the District Court (Biggs, C. J., R. 34). That conclusion is dictated by the plain language of the Act itself; it is reinforced by a consideration of the judicial and legislative context in which the Act was passed; the Commission has repeatedly so construed the Act; and the construction is supported by the existing authorities, including the decisions of both the lower courts in this case.

VIII

The only valid grounds upon which a remand of this case to the Commission can be predicated are either that as a formal matter, even though $100 per share is the most the preferred stockholders may lawfully receive, the Commission must approve the payment of only $100 to them before that portion of the plan can be enforced; or that as a substantive matter, the Commission could, on this record and on a proper rationale, lawfully authorize the payment to the preferred of more than $100 per share. Neither ground is here present.

As a formal matter, the Commission has already given its approval to the payment of only $100 to the preferred should it be decided that this sum is the most they can lawfully receive.

As a substantive matter, $100 per share is the most the preferred stockholders may lawfully receive. This conclusion follows from our contentions that the liquidation which here occurred was within the purview of the liquidation provisions of Engineers charter and the "fair and equitable" standard requires enforcement of those

charter provisions. It follows also from our contention that even if this is deemed not to have been a liquidation within the purview of the charter, the "fair and equitable" standard precludes payments to senior security holders who are being paid off in cash in the course of a genuine liquidation of more than the face amount of their claims.

Finally, this conclusion also follows from our contentions that, even if under some circumstances the holders of senior securities whose retirement is compelled by the Act may receive the "equitable equivalent" of rights surrendered, the Commission erred in appraising the "equitable equivalents" of the rights here surrendered, and the District Court had the authority to conclude, and properly concluded, that the "equitable equivalents" which the preferred are entitled to receive could not, on this record, exceed $100 per share.

ARGUMENT

PART ONE

IN A GENUINE LIQUIDATION SUCH AS TOOK PLACE HERE, THE "FAIR AND EQUITABLE" STANDARD REQUIRED THAT THE PREFERRED STOCKHOLDERS BE LIMITED TO $100 PER SHARE, PURSUANT TO THE CHARTER PROVISIONS, CONTROLLING PRECEDENTS, AND CONSTITUTIONAL LIMITATIONS.

I. Where a genuine liquidation has taken place, as here, the "fair and equitable" standard of Section 11(e) does not permit payment to stockholders in excess of the amounts authorized by the provisions of the corporate charter specifically applicable to such liquidation.

Both Courts below ruled that the Commission had misconstrued the doctrine of "equitable equivalents" which this Court in *Otis & Co.* v. *S. E. C.*, 323 U. S. 624, had deemed applicable in measuring the rights of security holders in the particular corporate dissolution there compelled by the Act. The District Court, therefore, did not deem it necessary to pass on the question whether, in contrast to the situation presented in *Otis*, the charter liquidation provisions applied to the liquidation here occurring and should be enforced. It held that the charter liquidation provisions were "but one circumstance looking toward non-payment of premiums" (R. 288a, 317a). The Court of Appeals stated without discussion that, in the light of the *Otis* decision, it considered that the charter liquidation provisions were not "dispositive of the issues presented" (R. 34), although it regarded the liquidation which here took place as significantly different from the one dealt with in *Otis* (R. 36).

Although we are in full accord with the grounds on which both Courts below found the proposed premium payments unfair and inequitable, we urge here, as we did below, that the charter provisions are specifically applicable to this liquidation and must be enforced in deference to the principles of "fairness and equity." and when so applied are dispositive of the issues.

A. The "fair and equitable" standard of Section 11(e) is predicated upon adherence to contractual rights.

If not for the authority which the Commission professes to find in the "fair and equitable" standard of Section 11(e), there could be no question that the distribution of Engineers'. assets to its security holders would be required to conform to the mandate of Engineers' charter. The forced dissolution of a corporate enterprise pursuant to an "overriding public policy" has, in no other context, been thought to require any alteration in the applicable charter claims of the security holders on dissolution. Compare *Continental Insurance Co.* v. *United States*, 259 U. S. 156. The question here, therefore, is whether the "fair and equitable" standard of Section 11(e) authorizes the Commission to alter the applicable charter liquidation rights of one class of security holders at the expense of another when the mandate of the Act requires the termination, rather than merely "simplification" of the holding company enterprise, and the final, rather than intermediate, distribution of its assets to its security holders.

We start with the proposition that the term "fair and equitable" in Section 11(e) of the Act is a term of art embodying the definite concepts which have been evolved for that term in the long history of equity receiverships

and reorganization statutes (*Otis & Co.* v. *S. E. C.*, 324 U. S. 624, 634). Until the *Otis* decision, that history left no doubt that "the touchstone of the 'fair and equitable' standard" was "the recognition of contractual rights" (*Federal Water Service Corp., et al.* 8 S. E. C., 893, 909). The rights of senior and junior security holders alike were held to stem from the contract defining the terms of their joint investment, and "fair and equitable" treatment required those contractual rights to be enforced "strictly" in any reconstitution of the enterprise through "receivership" or "reorganization" (*Case* v. *Los Angeles Lumber Co.*, 308 U. S. 106; *Consolidated Rock Products Company* v. *DuBois*, 312 U. S. 510; cf. *Bailey* v. *Minsch*, 168 F. 2d 635, 637 (C. C. A. 1, 1948) *cert. den.* 69 S. Ct. 83 (1948)).

To be sure, in reorganizations of continuing enterprises —whether solvent or insolvent—the "fair and equitable" standard does not require the payment of cash in satisfaction of security holder claims. (*Case* v. *Los Angeles Lumber Co., supra*, at 117). Such claims may be satisfied by the payment in new securities which are the "equitable equivalent" of the interests being surrendered (*Group of Investors* v. *Milwaukee R. Co.*, 318 U. S. 523, 565-566). But the reason for permitting payment in new securities, rather than in the cash required by the literal language of the contract, lies in the fact that the enterprise is continuing; because "practical considerations" might make it "impossible" for the reorganized enterprise to continue if the claims of the senior security holders are paid in cash (*Case* v. *Los Angeles Lumber Co., supra*, at 117), "fairness and equity" authorize the senior security holders to be awarded the "equitable equivalent", in new securities, of their contractual claims.

However, at least in reorganizations, this "equitable equivalent" can never exceed the cash amount of those claims. Compare *Knight* v. *Wertheim & Co.*, 158 F. 2d 838, 843 (C. C. A. 2, 1946), *cert den. sub. nom. McGuire* v. *Equitable Office Bldg. Corp.*, 331 U. S. 818 (1947); *Bailey* v. *Minsch, supra.* And we are not aware of any decisions which even suggest that if, in such reorganizations, security holders are being paid out in cash, they are entitled to payments greater than the amount of their contractual claims applicable to involuntary liquidation or retirement of their security.[1] On the contrary, any such intimation by a litigant has been rejected by the Courts (*Knight* v. *Wertheim & Co., supra; Bailey* v. *Minsch, supra*) and opposed by the Commission.[2]

It is not alone this Court's repeated insistence upon strict enforcement of applicable contractual rights as the core of the "fair and equitable" standard that impels the conclusion that Congress intended applicable charter liqui-

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[1] Indeed, even in appraisal proceedings incident to mergers where it is recognized that it is the voluntary act of the company which causes the retirement of the dissenting preferred stockholders from the enterprise, it has been held that their involuntary liquidation claim is the maximum which they may receive. *Matter of Fulton*, 257 N. Y. 487, 178 N. E. 766; *American General Corporation* v. *Camp*, 190 Atl. 225 (Md. 1937).

[2] Thus in rendering its advisory report to the District Court under Chapter X of the Bankruptcy Act, the Commission stated in *Matter of Childs Company*, Corporate Reorganization Release No. 67 (Sept. 30, 1946), p. 43:

> "The Trustee has taken the position that participation by the preferred stock is to be measured by its liquidation preference. The preferred stockholders are of the view that they are entitled to the investment value of their securities, which they claim is greater than the liquidation preference, primarily because of the non-callable feature of this preferred stock bearing a 7% dividend. We believe that the Trustee's position is sound."

dation provisions to control in authentic liquidations caused by the Act, although it is plain, as this Court indicated in *Otis,* that Congress intended the term "fair and equitable" as employed in Section 11(e) to carry its traditional and settled meaning. The repeated references to *Continental Insurance Company* v. *United States,* 259 U. S. 156, both in the report of the Senate Committee[1] recommending enactment of this statute and the statements of the proponents of the bill,[2] leave no doubt that at least when a genuine liquidation is compelled by the Act, the impact of this statute was intended to be no different from the impact of other legislation compelling corporate dissolution in the interest of an overriding public policy. The terms of the charter, to which junior and senior security holders bound themselves, mark the outer limits of what the senior security holders may receive in cash.

B. The liquidation of Engineers and the retirement of the preferred stocks came squarely within the purview of those provisions of the charter limiting the preferred stockholders to payment of no more than $100 per share.

The provisions of Engineers' corporate charter authorized the payment to the preferred stockholders of only $100 per share plus accrued dividends "in the event of any liquidation, dissolution, or winding-up of this corporation, or any reduction of its capital stock, resulting in any distribution of its assets to its stockholders"; provided, however, that if such liquidation, dissolution or winding-up or reduction shall have been "voluntary", the preferred stockholders would also receive certain redemption premiums, before any "distribution of * * * [the corpora-

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[1] S. Rep. No. 621 to accompany S. 2796, 74th Cong., 1st Sess., p. 33.

[2] H. R. Rep. 1318, 74th Cong., 1st Sess., pp. 49-50; 79 Cong. Rec. 4607, 8432.

tion's] assets shall be made to the holders of the common stock". The charter further provided explicitly that the preferred stockholders "shall be entitled to no further participation" in the distribution of assets upon liquidation, dissolution or winding-up or reduction of the capital stock accompanied by a distribution of assets, and that "all of the remaining assets of this corporation" are to be distributed to the common stockholders.[1]

In view of the findings of the Commission and both Courts below, there is no question that the liquidation of Engineers embodied in its Section 11(e) plan was dictated by the necessity of complying with Section 11 of the Act, and therefore was not "voluntary" within the meaning of the above charter provisions.[2] Accordingly, the preferred stockholders, having received $100 per share plus accrued dividends, are entitled under the charter to "no further participation in the distribution" of Engineers' assets unless what has taken place is not "a liquidation, dissolution or winding-up of this corporation or * * * reduction of its capital stock, resulting in any distribution of its assets". Clearly, both in letter and spirit, not merely one of these but all of them have occurred.

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[1] Appendix B, *infra*, pp. 166-7.

[2] Commission opinion, R. 48a (quoted, *supra*, pp. 9-10) District Court conclusions, Nos. 1-2, R. 315a-316a. Court of Appeals opinion, R. 36. The Commission and Courts have consistently held that reorganizations or liquidations such as this pursuant to Section 11(e) are not voluntary, even though formally "the company * * * takes the initiative in a proceeding under § 11(e)" L. Hand, J., *Public Service Commission* v. *S. E. C.*, 166 F. 2d 784, 787 (C. C. A. 2, 1948), cert. den. 334 U. S. 838; *City National Bank & Trust Co.* v. *S. E. C.*, 134 F. 2d 65 (C. C. A. 7); *In re Standard Gas & Electric Co.*, 151 F. 2d 326, 327 (C. C. A. 3), cert. den. 327 U. S. 796; *Cities Service Power & Light Corp.* Holding Company Act Release No. 4944; *Consolidated Electric & Gas Co.* Holding Company Act Release No. 4900, approved and enforced 55 Fed. Supp. 211 (D. Del., 1944).

Although the Commission's opinion did not find, or even suggest, that Engineers' dissolution was not a "liquidation, dissolution or winding-up" within the meaning of the charter, in the courts the Commission's counsel have joined the other respondents in intimating that Engineers' dissolution is not really a "liquidation" because, by the distribution of common stocks of the three operating companies to Engineers' common stockholders [1], the "enterprise" continues in fact, albeit in another form.

The answer to this contention is not only that both Courts below found explicitly that the dissolution of Engineers and the distribution of its assets among its security holders is a complete and final liquidation of the entire enterprise—both of the holding company and of the system [2]—but the barest rehearsal of the facts leaves no doubt as to the correctness of these findings. Engineers, an enterprise which had owned, directly and indirectly, and controlled and managed the activities of seventeen electric and gas utility and non-utility subsidiaries operating in fifteen states, has been completely dissolved. All but three of Engineers' subsidiaries have been sold for cash or liquidated in compliance with the Commission's orders, and this cash, together with the stock of the remaining three subsidiaries, has been distributed to the thousands of security holders of Engineers.

Plainly, the vast holding company, as it existed before the Act, was not a mere formal device through which each

[1] Actually only the stocks of Virginia and El Paso were distributed as a liquidating dividend; the common stock of Gulf States was purchased by the common stockholders by payment of $22,000,000 cash on the exercise of the Gulf States warrants. It will also be recalled that the common stocks of each company represent only a minority of the total capitalization of each company (*supra*, p. 7, n. 3).

[2] R. 316a, R. 36.

shareholder became a *pro rata* beneficial owner of shares of stock in operating companies. If all that was desired was ownership of operating utility common stocks, many excellent ones were freely available for purchase by any investor on the various stock exchanges. The stockholders who purchased shares of Engineers invested in a large holding company enterprise whose very essence was centralized control and management[1] of geographically diversified operating companies under the sponsorship of one of the world's oldest and most famous utility engineering firms;[2] that enterprise carried all the advantages associated with such a holding company: a large and expert central service organization,[3] combined mass purchasing power, favorable access to the best sources of finance, a leveraged capital structure, broad economic and geographic diversity,[4] and other significant economic benefits including tax savings resulting from consolidated tax returns.[5]

Instead of their investment in such an enterprise the security holders of Engineers, as a result of this proceeding, have received cash and/or the common stock of three isolated and unrelated operating utility companies. It requires no elaborate argument to demonstrate that termination of their investment in Engineers is no mere reorganization or formal shifting of an investment in an

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[1] See *North American Co.* v. *S. E. C.*, 327 U. S. 686, 701 (1946); see also Sections 1(b) and 2(a)(7) of the Act.

[2] See, for example, Engineers Exhibits 37-N to 37-P, R. 1650a, 1655a, 1665a.

[3] Engineers Exhibits 37-B, 37-C, R. 1446a-1448a, 1466-1468a.

[4] Engineers Exhibits 37-N, 37-O, 37-P, R. 1648a, 1654a, 1660a; Findings of Fact Nos. 3-6, R. 294a-295a.

[5] See *infra*, p. 96, n. 1.

otherwise continuing enterprise.[1] It is in fact what it is in form—a complete and final liquidation of the enterprise in which the security holders originally invested and a distribution in kind of the assets remaining in that enterprise after a substantial portion of the original assets have been sold for cash.[2] Indeed, if the present dissolution of Engineers is not a complete liquidation of the entire system, it is difficult to envisage what type of dissolution of the company and distribution of its assets—short of a piecemeal sale of the generators and power lines of the subsidiaries—would come within the charter provisions.

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[1] Cf. *In re Westerfield's Estate,* 82 N. Y. Supp. (2d) 766, — Misc. — (1948). See also, Commissioner Healy, dissenting in *United Light-American Light & Traction Co.,* Holding Company Act Release No. 6603 (1946), p. 41.

[2] Any intimation that this final distribution of portfolio assets constituted some sort of artful device for "continuing the enterprise" in the hands of "controlling" common stockholders must be set down as pure fantasy, devoid of any support either in fact, or in the findings of the Commission or the Courts below. Not only were the larger common stockholders also among the largest holders of the preferred (*supra,* p. 9, n. 2), but the fact is that large amounts of the portfolio stocks distributed in the liquidation have been sold by their original recipients and a substantial additional volume of sales is made each day on the New York Stock Exchange. A tabulation from Standard & Poor's Stock Guide establishes that approximately 800,000 shares of Virginia common and 550,000 shares of Gulf States were sold on the New York Stock Exchange subsequent to distribution and prior to November 30, 1948. These shares necessarily represent a portion of those distributed, since none were outstanding prior to the distribution.

Distribution of portfolio assets as a liquidating dividend is, of course, a common incident of many corporate liquidations. In fact, Engineers attempted to sell one of these three remaining assets for cash, but was unsuccessful in its attempt (Engineers Ex. 37-K, R. 1609a). Under the circumstances, it was only logical for the management of Engineers to distribute the remaining stocks pro rata to the stockholders, in the manner provided by the charter, thus avoiding underwriting and selling expenses, and leaving it to each stockholder to decide whether and when to sell his pro rata share in accordance with his own financial needs and judgment (R. 644a).

It does not detract from this conclusion that the Public Utility Holding Company Act had not been enacted in 1925, at the time when Engineers' charter was drafted. In point of fact, it was widely known at that time that legislative efforts were being made to bring about the curtailment and dissolution of the "power trusts" and "power monopoly" represented by public utility holding companies. By 1924 the halls of Congress and the pages of many sections of the public press resounded to almost continuous attacks upon "the power trust" and the "power monopoly" and demands for remedial action against utility holding companies.[1] Under the pressure of a group of "anti-power trust Senators", led by Senators Walsh of Montana and Norris of Nebraska, the United States Senate in December, 1924, launched the first of a series of sweeping congressional investigations of utility holding companies which culminated directly and proximately in the adoption of the Act.[2] These investigations were ac-

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[1] Cf. Bonbright & Means, The Holding Company (1932):

> "It was in the field of local public utilities that the holding company has reached its highest stage of development, and *it is in this field also that this corporate device has been subject to the most severe criticisms from spokesmen for the public interest*" (p. 190; emphasis supplied).

[2] See Senate Resolution 329, 68th Cong., 2d Sess.; Senate Resolution 83, 70th Cong., 1st Sess.; see, also, recitals in Section 1(b) of the Act.

During the Congressional debates on the Holding Company Act, Senator Wheeler stated:

> "* * * let me call the Senate's attention to the fact that this bill is not something new. It is the outgrowth of an investigation which was started in Congress a great many years ago when my colleague, the late Senator Walsh, one of the greatest lawyers who ever served in this body, started the investigation into the holding companies which was continued before the Federal Trade Commission, where for 6 or 7 or 8 years they have been conducting the investigation" (79 Cong. Rec. 8384; 74th Cong., 1st Sess.).

companied by startling events and disclosures whose reverberations were featured almost continuously in the public press of the time.[1]

It is in the light of these widespread public attacks on the power trusts that the language of Engineers' charter assumes particular significance. The charter expressly contemplates a "reduction of * * * [the corporation's] capital stock, resulting in any distribution of its assets to its stockholders". Whatever else such a provision may embrace, it certainly covers both the distribution of portfolio assets pursuant to the compulsion of the anti-trust or other relevant laws curtailing or dissolving the "power trusts" and the sale of subsidiaries under such legal compulsion and distribution to the stockholders of the cash proceeds of such sales. While those who drafted this clause could not have known of the precise form of curtailment of holding company operations ultimately to be embodied in the Public Utility Holding Company Act, it is plain that the clause does cover all such types of system curtailment or liquidation, even *partial*, by force of law.

It is undisputed that Engineers has, pursuant to explicit orders of the Commission, sold a substantial portion of its assets for cash, and has in these proceedings used that cash to retire its preferred stock under the compelling impact of the statute.[2] Hence, even if it be contended that

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[1] Set forth at the end of this brief as Appendix C, *infra*, pp. 168-175, are a few representative items which appeared in the press of the period. These examples could be multiplied many fold.

[2] See the Commission's admonition to Engineers to reduce its capitalization or face the probability of mandatory action by the Commission under Section 11(d) of the Act, in *The Western Public Service Company*, 12 S. E. C. 804, 808; and the pointed references in the concurring opinion to the "reduction of capital" provision of the charter (pp. 819, 820).

In the light of the Commission's repeatedly announced policies affirmed by the Courts, reduction of the capital of a holding company such as Engineers, whose subsidiaries had large amounts of bonds and preferred stocks outstanding, necessitated the complete

the present proceedings have not produced a complete "liquidation" of the company—a contention itself devoid of all merit—it is nevertheless inescapable that they have produced at least a "reduction of its capital stock, resulting in * * * [a] distribution of its assets to its stockholders". By the explicit terms of the charter such a reduction of capital permits the preferred stockholders to be paid no more than $100 plus accrued dividends.

It is doubtless for these reasons that the Commission did not even intimate, in its opinion, that the existence of Engineers and of its holding company system was not being terminated, or that the enterprise was not being definitively "liquidated". Nor did the Commission, in its opinion, base its conclusion that the preferred stockholders should receive more than $100 per share on any finding that this was not in fact a "liquidation" within the meaning of Engineers' charter. On the contrary, what it said was merely that "the liquidation provisions of the charter" are not "conclusive". Having said that, it proceeded to ignore those provisions completely.[1]

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elimination of the holding company preferred stocks. Cf. *Commonwealth & Southern Corp.*, 9 S. E. C. 609 (1941), aff'd *Commonwealth & Southern Corp.* v. *S. E. C.*, 134 F. 2d 747 (C. C. A. 3); *Central and Southwest Utilities Co.*, 11 S. E. C. 533, aff'd *Central and Southwest Utilities Co.* v. *S. E. C.*, 136 F. 2d 273 (App. D. C.); *Consolidated Electric and Gas Company*, Holding Company Act Release No. 4900 (1944), approved and enforced, 55 F. Supp. 211 (D. Del., 1944); *Cities Service Power & Light Corp.*, Holding Company Act Release No. 4944, p. 15 (1944).

[1] Since the Commission determined the value of the preferreds solely on the basis of Badger's estimate of the price at which they would have sold on the market if their retirement had not been compelled by the Act (*infra*, pp. 74-86), the amount of their charter liquidation claim was accorded not even the slightest weight. Under the Commission's approach, the amount awarded the preferred would have been no different if the liquidation provision of the charter specified $110 per share in all dissolutions (as certain holding company charters do specify), instead of the $100 actually specified here.

C. Nothing either ruled or said by this Court in the *Otis* case alters the command of the "fair and equitable" standard that the contractual relationship be strictly enforced.

Being unable to find that the present liquidation of Engineers is not within the liquidation provisions of its charter, the Commission, in reliance on this Court's decision in the *Otis* case, and perhaps in *Schwabacher* v. *United States,* 334 U. S. 182, claims the power, on the forced liquidation of a solvent corporation or retirement of its senior securities, to award to senior security holders cash amounts in excess of their contractual claims. Respondents submit that the Commission's reliance on these cases for support of such a proposition is grossly misplaced.

The crucial fact, upon which both the Commission's opinion and this Court's decision in *Otis* rests, is that the holding company enterprise continued essentially unchanged, even though the particular corporation there involved was being dissolved pursuant to the mandate of the Act, as an incident to the simplification of the continuing system. As the Commission repeatedly pointed out, both in its opinion [1] and in its brief in this Court, [2]

[1] See *United Light & Power Company,* 13 S. E. C. 1 (1943).

[2] See Brief of S. E. C., October Term 1944, No. 81, at pp. 78-79:

"Finally, in no realistic sense is there occurring *in this case* a dissolution of a business enterprise which should call for the application of a charter liquidation preference. As the opinion of the majority of the Commission discloses, the preferred and common stockholders of Power have been the residual co-owners of a vast public-utility system controlled through Power, the top holding company, and Railways its principal *subholding company subsidiary.* These stockholders will continue to remain the residual owners of *the same public utility system* * * *. *In essence, therefore, while Power is being dissolved the enterprise is not*" (emphasis supplied).

Similarly, Professor Dodd, whose article is referred to in the majority opinion of this Court (p. 630) had repeatedly stressed the mere simplification of a continuing holding company system involved in the *United Light* case. Dodd, *Holding Company Act Recapitalizations* (1944), 57 Har. L. Rev. 295, 308, 313.

all that happened there was that the top company in a multi-tiered holding company system was eliminated, and its security holders were given the securities of the second holding company in the continuing system in lieu of their holdings in the top company.

Not only was it thus urged, and found, as a fact [1] that both the holding company enterprise and the participation of the preferred stockholders in it continued, but the doctrine which the Commission evolved and this Court approved in that case to measure how a "fair and equitable" distribution of assets was to be achieved, was predicated upon this continuance of the enterprise in fact. "Equitable equivalence" was computed by estimating the future earnings of the continuing enterprise available for each class of security holders—precisely the valuation technique which the continuance of the enterprise required. Cf. *Consolidated Rock Products Co.* v. *DuBois*, *supra*, at 525-526.

Because, in fact, there was no liquidation, fairness and equity did not require the Commission to enforce the charter liquidation rights of the preferred stockholders; in the absence of an authentic liquidation those rights did not come into play.[2] It would not be "fair and equitable"

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[1] See, e.g., 323 U. S. 628-629, 631-637; 142 F. 2d 411 (C. C. A. 3); 51 F. Supp. 217 (D. C. Del.).

[2] As this Court stated: "There is an argument that if the charter provision applies to this situation it cannot be disregarded and that in such a liquidation 'fair and equitable' would require the distribution of assets only to the preferred. *We do not* reach that question. *The point at issue is whether this charter provision applies*" (323 U. S. 624, 635-636; emphasis supplied).

Apart from the fact that here, unlike *Otis*, a genuine and final termination of the holding company enterprise has occurred, the provisions of Engineers' charter are significantly different from those of the charter involved in the *Otis* case. There is no room here for the argument that the term "involuntary liquidation" employed in cor-

to accelerate or "mature" the liquidation rights of the preferred stockholders at the expense of the common stockholders, since the enterprise and the participation of the preferred therein were to continue and the Commission had expressly found that "* * * the whole future program of corporate simplification and geographic integration of the system * * * will result in an improvement of the investment position of both the preferred and the common stock. That improvement we believe should be shared by the common as well as by the preferred, and the process of securing such improvement in compliance with the Act should not be permitted to destroy existing investment values." [1]

In *Schwabacher* v. *United States*, 334 U. S. 182, as in the *Otis* case, the power of a Commission to transmute preferred stockholders' rights into their "equitable equivalents" was affirmed. But this power was found to exist only because the enterprise which state law would regard as "liquidated" was in fact continuing, augmented

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porate charters as a term of art is limited to bankruptcy or creditor proceedings, or at least to the types of involuntary liquidation which were foreseeable when the term was inserted in the charter. Engineers' charter does not use the term "involuntary liquidation". It prohibits the payment of premiums on "liquidation", unless it is affirmatively shown that the liquidation was "voluntary". In the second place, as we have stated, the type of retirement of preferred stock here occurring, even without reference to the accompanying liquidation of the company, was itself within the contemplation of the liquidation clause which in addition to the provisions for "liquidation", "dissolution" and "winding-up" provided for "any reduction of [the corporation's] capital stock" resulting in any distribution of its assets to its stockholders, a provision wholly absent from the charter contained in *Otis*.

[1] 13 S. E. C. 1, 19 (1943), quoted in the Commission's brief (*supra*, p. 45, n. 2) at p. 20.

by merger, and the preferred stockholders' investment in that enterprise likewise continued.[1]

Above all, the *Otis* decision reflects the determination of this Court and the Courts below (the very ones which also passed on the case at bar) to cut through surface technicalities and pierce to the substantive realities of the question. The very essence of the *Otis* decisions in all three Courts was the refusal to apply liquidation standards to a mere simplification and reorganization of a continuing holding company system. *Schwabacher* v. *U. S.*, supra, was a reaffirmation of that same insistence upon dealing with realities by refusing to hold that matured liquidation claims were the measure of dissenting stockholders' rights in a continuing railroad enterprise augmented by merger. Yet here the Commission seeks to rely on these decisions for justification in applying wholly *fictional* (and erroneous, as will be shown) reorganization standards to an incontestably authentic and final liquidation.

In sharp contrast to *Otis* and *Schwabacher*, this case involved a genuine liquidation and distribution of assets of an entire holding company system and the final termination of the investment which the security holders had made in it. In terms and in fact, therefore, the liquidation provisions of the corporate charter applied to this situation. And here the preferred stockholders were

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[1] "*Since the federal law clearly contemplates merger as a step in continuing the enterprise* it follows that what Michigan law might give these dissenters on a *winding up or liquidation* is irrelevant except insofar as it may be reflected in current values for which they are entitled to an equivalent. It would be inconsistent to allow state law to apply a liquidation basis to what federal law designates as a basis for continued public service" (*Schwabacher* v. *U. S.*, 334 U. S. 182, 200; emphasis supplied).

repaid their full investment entirely in cash, rather than being required to accept new securities representing another form of continuing interest in the holding company system, as were the preferred stockholders in *Otis*.

Since the Act compelled the relinquishment by the preferred stockholders of their interest in an enterprise which was being liquidated, and freed them from the risks of a new enterprise, their rights were to be measured as on liquidation, not as though they remained participants in a continuing enterprise.[1] The abrupt impact upon the stockholders of the "overriding public policy" embodied in the Act may render it appropriate for the Commission to transmute the surrendered claims of senior security holders into their "equitable equivalents" when they are forced by the Act to remain part of a continuing enterprise; but nothing in the Act or its history authorizes, or makes it appropriate for, the Commission to enhance the contractual rights of senior security holders when a genuine liquidation compelled by the Act relieves them of all the risks of the continuing enterprise.[2] In those circumstances

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[1] In plain recognition of the distinction between a senior security holder's continuing interest in a continuing enterprise and his interest when severed from the enterprise by being paid out in cash, Congress, in bankruptcy and reorganization legislation, has provided that senior security holders who are paid off in cash are wholly excluded from voting on the plan of reorganization (Bankruptcy Act, Sec. 77(e); Ch. X, Secs. 179, 222). Because those being severed from the enterprise under the impact of bankruptcy receive in cash the full amount of their retirement or liquidation claim, they are no longer "affected" by the plan under which the enterprise continues, and are not permitted to vote on it.

And the amount of the cash payment is limited to the involuntary liquidation claim or face amount of the security, plus arrears of dividends or interest (cf. *Knight* v. *Wertheim, supra,* p. 36; *The United Light & Power Co.,* 10 S. E. C. 1215, 1225).

[2] Cf. Brief of S. E. C. in *N. Y. Trust Company* v. *S. E. C.,* 131 F. 2d 274 (C. C. A. 2), quoted *infra*, p. 56, n. 1.

"fairness and equity" entitle the senior security holders to no more than is provided for them in the applicable provisions of their charter.[1]

If, as has been stated, the dissolution of Engineers and paying off of its preferred stockholders is claimed not to have been a "liquidation, dissolution or winding-up" of the enterprise (and we submit that it indisputably was), it was beyond cavil at least a "reduction of its capital stock, resulting in * * * [a] distribution of its assets to its stockholders". In either event, what occurred was plainly within the provisions of the charter which limit the preferred stockholders to receiving $100 together "with all dividends accrued or in arrears thereon" and to "no further participation in * * * [the] distribution" of its assets. Under the charter the common stockholders receive "all of the remaining assets". Execution of that charter is the command of fairness and equity.

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[1] Indeed, the Commission itself early recognized that the distinction between "liquidation" of the enterprise and of the senior security holders' interest in it, on the one hand, and a mere alteration in the senior security holders' investment in a continuing enterprise, on the other, was embodied in the "fair and equitable" standard of Section 11 of the Act. And the Commission unequivocally asserted that, while because of this distinction it was authorized to transmute into "equitable equivalents" the relinquished prior claims of senior security holders in a going concern in which they were obliged to remain, the "fair and equitable" standard contained no authority for such transmutation in avoidance, if not violation, of contractual liquidation provisions when the enterprise was being liquidated and its preferred stockholders paid off. *Federal Water Service Corp. et al.*, 8 S. E. C. 893, 907-911.

II. Even if Engineers' dissolution pursuant to the Plan under consideration is deemed not to have been within the purview of the charter liquidation provisions, the "fair and equitable" standard, as interpreted in a long series of Commission and Court decisions, precluded the payment to the preferred stockholders of more than $100 per share.

We have contended that because a genuine and final liquidation of Engineers has taken place, the terms of the charter liquidation provisions limit the preferred stockholders to $100 per share plus dividends, and the "fair and equitable" standard requires enforcement of those terms. If, however, notwithstanding this contention it is held that the charter liquidation provisions were not applicable to the instant liquidation, we submit that nevertheless "fairness and equity" interdicted any award to the preferred stockholders of more than $100 per share.

The instant case was not the first in which the Commission was faced with the problem of determining the rights of senior security holders to premium payments upon the forced liquidation of their enterprise or the retirement for cash of their securities, where the contractual provisions were deemed not applicable. When first this question was presented, the Commission concluded that the "fair and equitable" treatment commanded by the Act dictated the application of the established equitable doctrine of frustration—i.e., that frustration of the enterprise by governmental acts or other supervening events not provided for by the parties required "the loss * * * [to] * * * lie where it falls. Neither party can be com-

pelled to pay for the other's disappointed expectations."[1] And, on the other hand, neither party will be permitted to retain moneys paid by the other on account of an executory contract which has been frustrated. This deeply rooted principle, which some forty years before enactment of the Holding Company Act had been held applicable by the courts in determining the rights of stockholders of a corporation dissolved under the compulsion of law,[2] was found by the Commission to be part and parcel of the "fair and equitable" standard of Section 11(e)—in the very liquidation which gave rise to this Court's decision in the *Otis* case. Thereafter this principle has been repeatedly applied by the Commission and by the courts in a long and hitherto unbroken line of decisions.[3]

In the liquidation of United Light & Power Company, the Commission ruled, and was upheld by this Court in the *Otis* decision, that as between the preferred and common stockholders, since both were receiving stock in the continuing enterprise, "fairness and equity" required each to receive the "equitable equivalent" of that which he was being compelled to give up.[4] But the debenture holders, who were being retired from the enterprise by the payment of cash, were held precluded by "fairness and equity" from receiving any added compensation or "equi-

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[1] American Law Institute, Restatement of the Law of Contracts, Sec. 468 (Comment on subsection 3, page 887); also see 6 Williston on Contracts (revised ed. 1938), Sec. 1938 et seq.

[2] *Lorillard* v. *Clyde*, 142 N. Y. 456 (1894). In that case the principle was held applicable to a contract in which the junior security holders exercising full control and management of the enterprise specifically guaranteed the future payment of dividends to the senior security holders.

[3] Cases collated, *infra*, p. 55, notes 3 and 4.

[4] *United Light & Power Co.*, 13 S. E. C. 1 (1943).

table equivalent" for the 6% and 6½% claims on future earnings in the form of secure interest payments which they were required to relinquish. However lucrative would have been the return on their investment if permitted to remain outstanding, they were held entitled to receive only the face amount of their securities, which represented theoretically the amount they originally had contributed to the enterprise. In denying the debenture holders' right to receive the premiums to which they were entitled upon voluntary retirement of the debentures before maturity, or added compensation of any kind for the loss of their future high interest payments, the Commission stated:

> "We believe that the obligation to pay a premium was intended to arise only when the company was to continue as a going concern, for the payment thereof is in the nature of compensation payable by the company (i.e., its stockholders) to the debenture holders for depriving the latter of their investment. In a going concern, the stockholders may be deemed to benefit from the elimination or reduction of the debt effected by the redemption, and the premium may be regarded as the prearranged amount payable by them for such benefit.
>
> "But here the company does not continue as a going concern. There is no question of free choice or election. The company by virtue of congressional mandate is to terminate its existence. Power must liquidate not only its debt but also its stock. The rights of debenture holders and stockholders alike to retain their respective investments are cut off." *The United Light & Power Co.*, 10 S. E. C., 1215, 1221 (1942).

The Commission then went on to state (p. 1223):

> "* * * we are impelled to the conclusion that the terms of the debentures and the covering agreements

create no contractual obligation on the part of Power to pay a redemption premium and no right on behalf of the debenture holders to receive such premium. *We further conclude that no such obligation or right exists by virtue of any other recognized legal or equitable principle.*" (Emphasis supplied.)

And in holding that neither legal nor equitable principles entitled the debenture holders to more than the principal amount of their securities, the Commission had squarely before it the contention of the bondholders that, wholly apart from contract rights, they should as a matter of "fairness and equity" receive additional compensation because they were being deprived prematurely of a valuable investment bearing interest rates of 6 and 6½%, rates so lucrative that the debentures had been selling at a premium above par.[1] The Commission disposed of this contention as follows:

> "Lastly, counsel for the debenture trustee argues that if the redemption provisions are held inapplicable so that the debentures are treated as being in effect non-callable, some compensation must still be given to the debenture holders for the termination of their investment. The call premium of 9 percent is suggested as *an appropriate measure of such compensation.* It seems to us *a complete answer* to this argument that the termination of the investments of debenture holders and stockholders alike has been brought about by the act of a sovereign power—in this case a congressional mandate. We think the debenture holders have established no right to receive such compensation here at the expense of the

[1] *The United Light & Power Co., supra,* p. 1227, n. 27.

stockholders, whose rights we must also consider." (Emphasis supplied.)[1]

On appeal, the Second Circuit affirmed the Commission's holding and recognized that, at least where contractual provisions were not applicable, the doctrine of frustration of the enterprise was part and parcel of the "fair and equitable" standard (*New York Trust Co. v. S. E. C.*).[2] Thereafter, this doctrine was consistently applied by the Commission and the Courts[3] to limit preferred stockholders and bondholders to the face amount of their securities in the numerous cases involving retirements of senior securities of holding companies required to liquidate in whole, or merely *in part*.[4]

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[1] *Id.* at p. 1228.

[2] 131 F. 2d 274 (C. C. A. 2, 1942), *cert. den.* 318 U. S. 786, *rehearing den.*, 319 U. S. 781.

[3] Not less than four different circuit courts of appeal have passed on the question and have uniformly held the frustration doctrine applicable. See, in addition to the decision of the Second Circuit in the *New York Trust* case, the following:

City National Bank & Trust Co. v. S. E. C., 134 F. 2d 65 (C. C. A. 7, 1943); *Massachusetts Mutual Life Insurance Co. v. S. E. C.*, 151 F. 2d 424 (C. C. A. 8, 1945), *cert. den.* 327 U. S. 795; *In re Standard Gas & Electric Co.*, 151 F. 2d 326 (C. C. A. 3, 1945), *cert. den.* 327 U. S. 796. Cf. *Bailey v. Minsch*, 168 F. 2d 635 (C. C. A. 1, 1948), *cert. den.* 69 S. Ct. —, 1948.

And in the District Courts, see: *In re Laclede Gas Light Co.*, 57 F. Supp. 997 (E. D. Mo., 1944); *In re North Continent Utilities Corp.* [illegible]4 F. Supp. 527 (D. Del., 1944); *In the Matter of Consolidated Electric & Gas Co.*, 55 F. Supp. 211 (D. Del., 1944); *In re Central States Power & Light Corp.*, 58 F. Supp. 877 (D. Del., 1944); *In re Interstate Power Co.*, 71 F. Supp. 164 (D. Del., 1947).

With respect specifically to retirement of preferred stocks without premiums, see *Cities Service Power & Light Co.*, Holding Company Act Release No. 4944; *Georgia Power & Light Co.*, Holding Company Act Release No. 5568; *El Paso Electric Co.*, Holding Company Act Release No. 5499.

[4] Thus, in *Cities Service Company, et al.* (Holding Company Act Release No. 4944 [1944]) the Commission held the doctrine appli-

Apart from its authoritative command as a part of the texture of the "fair and equitable" standard, the doctrine of frustration offers a peculiarly apt solution for the problem created by the forced retirement of senior securities in the liquidation of an enterprise pursuant to the mandate of the Act, when the provisions of the corporate charter are deemed not to cover such a contingency. In the situation in which "the enterprise continues" so that charter liquidation claims do not come into play and the senior security holders' participation is forced also to continue, there may be sound reasons, as this Court pointed out in the *Otis* case (p. 637), for not restricting either the Commission or the parties to one form of change rather than another. And "fairness and equity" may, in such circumstances, require an equitable adjustment in the relationship of the security holders who are forced to continue as partners in a going enterprise.[1]

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cable to retirement of the debentures and preferred stocks of a holding company which had not been ordered to liquidate but merely to divest itself of a portion of its properties pursuant to Section 11(b)(1). The same is true of the retirement of the notes and debentures of *Standard Gas & Electric* (*supra*) and of the senior securities in *Consolidated Electric & Gas Company* (Holding Company Act Release No. 4900 [1944]) approved and enforced: *In the Matter of Consolidated Electric & Gas Co.*, 55 F. Supp. 211 (D. Del., 1944). It also held the same doctrine applicable in the case of at least two operating companies which are necessarily continuing enterprises. *In re Laclede Gas Light Co.*, 57 F. Supp. 997 (E. D. Mo., 1944), aff'd *Massachusetts Mutual Life Ins. Co.* v. *S. E. C.*, 151 F. 2d 424 (C. C. A. 8, 1945); *Interstate Power Company* (Holding Company Act Release No. 7143, 1947), approved and enforced. *In the Matter of Interstate Power Co.*, 71 F. Supp. 164 (D. Del., 1947).

[1] As the Commission pointed out in its brief dated August 15, 1942, in the Second Circuit in *New York Trust Company v. Securities & Exchange Commission*, 131 F. 2d 274:

"Admittedly property rights of innocent security holders should be preserved upon the liquidation of a corporation under * * * [the anti-trust laws] * * * or under the present law. The question is what these rights are. [If] * * * capital funds

But when the final termination of the enterprise, or of the senior security holders' interest in it is compelled, and both senior and junior security holders are cut loose from their partnership relationship, each group of security holders is deprived of the reciprocal advantages which its investment in the joint enterprise gave it. Neither class should be permitted to obtain compensation from the other class for the loss of its "disappointed expectations".[1]

In short, a species of rescission by operation of law has occurred[2] and the face amount of the security—which theoretically mirrors the senior security holder's contribution to the enterprise—is all that he is entitled to recover.

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obtained from the issuance of the securities affected by the dissolution were not returned to the investors but were retained for the use of the successor corporations, * * * the investors would be thus required to accept other securities in different corporations, thereby keeping their investments tied up in other enterprises. [Compensation in those cases] * * * is not given for the loss of their investments, but for the continuation of their investments in successor companies at greater risks" (p. 29).

[1] Despite the fact that the Engineers' common stockholders did not benefit in even the slightest degree, and in fact lost heavily, as the result of the liquidation (*infra*, pp. 116-119) it may be observed that in applying the principle of frustration, the courts have consistently held that "the loss must lie where it falls" as a matter of sound policy even where the other party is unquestionably a beneficiary of the frustration. See, for example:

Omnia Commercial Co. v. *U. S.*, 261 U. S. 502; *The Isle of Mull*, 278 Fed. 131 (C. C. A. 4; 1921), *cert. den.* 257 U. S. 662; *Earn Line S.S. Co.* v. *Sutherland S.S. Co.*, 254 Fed. 126, 134, aff'd *sub. nom.*; *The Claversek*, 264 Fed. 276 (C. C. A. 2, 1920); *Nitro Powder Co.* v. *Canadian C. & F. Co.*, 233 N. Y. 294, 135 N. E. 507. See, also, The Gold Clause decisions: *Norman* v. *B. & O. R. Co.*, 294 U. S. 240; *Perry* v. *U. S.*, 294 U. S. 330; *Holyoke Water Power Co.* v. *American Writing Paper Co.*, 300 U. S. 324; *Smyth* v. *U. S.*, 302 U. S. 329; *Guaranty Trust Co.* v. *Henwood*, 307 U. S. 247.

[2] *Cf. Williston, Contracts, supra*, p. 52, n. 1, at p. 5486, n. 10.

That these are the principles which are embodied in the concept "fair and equitable" as used in the Act is made plain by the Commission's pertinent statement in its brief in the Second Circuit Court of Appeals in *New York Trust Co.* v. *S. E. C.*[1] (*supra*):

> "The petitioner's claim for compensation must, moreover, be considered in the light of *the correlative rights of Power and its stockholders.* Power had the right by contract to use the capital received from the debentures exclusively for itself, subject only to the payment of interest for its use. *The Holding Company Act and the Commission's order pursuant thereto have taken away this right. In these circumstances neither party is entitled to compensation for the loss of their correlative rights.* It is well settled that a promisee is not entitled to compensation for the loss of his bargain when the promisor has been denied his expected benefits under the contract through the impact of a supervening statute [citing cases]. (pp. 26-27).
>
> * * * Under these decisions Power must be considered free from liability to pay interest on the debentures in the future, *or compensation for the loss thereof,* because the statute has deprived Power of any benefits from the use of the capital. The debenture holders must, therefore, accept the premature termination of their rights under the agreements (p. 29).

* * * * * *

In the instant case *neither Power nor a successor company is retaining, or can retain, the capital obtained from the sale of the debentures for the benefit of the system.* The debenture holders are being

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[1] Brief dated August 15, 1942, on behalf of the Securities and Exchange Commission. (Emphasis supplied.)

repaid the principal of and accrued interest on their debentures, *are restored to their original position, and are not compelled to accept the risks of a new enterprise.* Under these circumstances, as we have heretofore shown, the debenture holders are not entitle to anything more" (p. 30).

This rationale, as the District Court specifically found, applies with special force to the facts of this case. Here, as in those other cases denying the payment of premiums to senior security holders, the preferred stockholders have, to be sure, relinquished a preferential claim to future dividends at a rate which they contend was attractive. But that same mandate which deprived the preferred stockholders of those future dividends simultaneously deprived the common stockholders of the valuable right to utilize the preferred stockholders' capital, which constituted the entire consideration for the payment of the dividends. Moreover, in this case, even more demonstrably than in the others, the junior security holders have suffered additional deprivations of a far-reaching character as a result of the statutory requirement to liquidate. Thus, although throughout the history of Engineers the preferred stockholders have received their stipulated dividends in full, aggregating approximately $90 per share,[1] the common stockholders had received no dividends whatever since 1932 (and a total of less than $5 prior thereto) notwithstanding that since the enactment of the statute in 1935 more than $24,000,000 had accrued

[1] District Court Finding No. 26, R. 303a. The Court pointed out that its figures were as of December 31, 1946; thereafter the preferreds received additional dividends until June 30, 1947, which have enhanced the sum mentioned above.

to the common's interest in earnings, and almost $10,-000,000 of this sum had been available for dividends on the common stock.[1] The common stockholders were required to forego all such dividends in order to provide for the adjustments required by the Act, including the statutory requirement embodied in Section 11(b)(2) that the company shrink its capital structure by retirement of the preferred stocks.[2] Since the funds thus accumulated through retained earnings and the proceeds of divestments were not sufficient to meet the contractual claims of the preferred, the common stockholders were required to supply $22,000,000 additional in cash for this purpose, through the exercise of "warrants" entitling them to receive their pro rata share of one of the company's assets in the dissolution.[3]

Moreover, the divestment of subsidiaries required by the Act had, as concurrent findings of both Courts below establish, resulted in large losses to Engineers as a company by compelling it to part with the stocks of subsidiaries at prices considerably under the prices realizable for those stocks if the company had not been required to comply with the Commission's divestment orders.[4] Even where the divestments did not produce an actual

[1] District Court Findings 33-35, R. 305a-307a; Engineers Ex. No. 30, R. 1395a; R. 470a; Cf. Commission Opinion, R. 69a.

[2] District Court Finding 37, R. 307a; Cf. Commission Opinion, R. 69a.

[3] District Court Findings 39-40, R. 308a-309a; Cf. Commission Opinion, R. 41a-43a.

[4] District Court Findings 37-38, R. 307a-308a; Court of Appeals Opinion, R. 34, 36.

book loss as of the time of divestment,[1] they deprived the company of the high earnings of the subsidiaries with which it was compelled to part.[2]

As a result, the common stockholders find themselves in the position of being deprived of the $39,000,000 of capital which the preferred stockholders had contributed for the company's use without any limitation of time,[3] losing the extremely high earnings which the enterprise had received from the investment of that sum,[4] and of having received no dividends for a period of some ten years because of the necessity for accumulating funds to retire the preferred stock under the compulsion of the statute.

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[1] The Commission recognized that these losses had occurred (R. 72a) but stated it did not "accept the hypothesis" that the Act had caused the losses, since Engineers was free "within limits" to choose the time for divestments. But those "limits" were very stringent indeed. Divestment orders not complied with within one year are subject to mandatory enforcement proceedings, including the appointment of a trustee. See Sections 11(c) and 11(d) of the Act. Although the Commission is authorized to grant an extension "for an additional period not exceeding one year", a corporation which delays in the carrying out of divestments is placed in the position of gambling on the Commission's benevolence or inaction.

The District Court's findings as to the losses were based upon uncontradicted evidence that Engineers would have been able to obtain much higher prices if it had not been compelled to carry out the divestments, or alternatively would have received higher earnings if it had retained the assets (cf. Finding 37, R. 307a-308a). The Court of Appeals having affirmed these "careful and far reaching findings" (R. 34, 36) we submit that these concurrent findings "are final here in the absence of very exceptional showing of error". *Comstock v. Group of Investors*, 335 U. S. 211, 214 (1948).

[2] District Court Finding 37, R. 307a, Court of Appeals, R. 36-37.

[3] Cf. Brief of S. E. C. in *New York Trust Co. v. S. E. C., supra*, p. 56.

[4] See discussion, *infra*, pp. 117-119, for the highly profitable employment of these funds which was denied to the common stockholders by the mandate of the Act.

On the other hand, the preferred stockholders having received repayment of something more than *the maximum amount* contributed by them or their predecessors to the enterprise[1] as well as dividends at the full contract rate to the date of retirement of the preferred, now demand that the common stockholders pay them an additional $3,200,000, for the relinquishment of their future right to assertedly high dividends. In a word, the preferred stockholders seek payment for their "disappointed expectations"; and they demand that the common stockholders become indemnifiers of this theoretical

[1] Two of the issues were sold to the public at the time of issuance for $100 per share, and the third at $99.50 per share, although t company actually received on the average something less than $96 per share for all three issues (District Court Findings Nos. 22-23, R. 301a). The $5 series carried the privilege of conversion until 1938 into common stock, a feature which obviously had substantial value independently of the preferred (large amounts of this stock were converted into common at an average price of $52 per share in 1928-1929, a period where the common sold as high as $79¾). The $5.50 series (sold to the public at $99.50 per share) carried a warrant giving the holder a "call" on common stock over a 10-year period (District Court Finding No. 22, R. 301a). It is thus evident that in paying approximately $100 the original purchasers of these stocks were paying something *less* than $100 for the stock alone, since the conversion features and warrants had substantial value in their own right.

As to those who purchased subsequent to the initial issue, it is to be noted that the market price of all three issues from date of issuance until virtually the date of retirement ranged between $63-$67, *averaged over the entire period* (Commission's Opinion, R. 62a-63a). The record establishes that turnover during the period of depressed prices (particularly during the years when the preferreds were selling in the range of $10-$15 per share) was extremely heavy. Over the entire period, the turnover ratio of the $5 series was 335%; of the $5.50 series, 215%; of the $6 series, 195% (see Engineers Exs. 26-28, R. 1391a-1393a).

future deprivation even though the common have themselves suffered great deprivations, both past and future.

If ever a case called for the tempered application of the principle that "neither party is entitled to compensation for the loss of their correlative rights",[1] we submit that this is that case.

By what process of reasoning then, did the Commission come to rule that in this case "fairness and equity" require payment by the common stockholders to the preferred stockholders of $3,200,000 in excess of the maximum capital contribution, charter and book claim of the latter? The Commission reached this result by indulging in the baldest fiction, and asserting a limitless power to determine what "fairness and equity" require. It "hypothesized" that the holding company enterprise was continuing despite the fact that it was not; and although the retirement of their securities for cash relieved the preferred stockholders of the risk of all potential unfavorable circumstances, the Commission held that the preferred stockholders should receive in cash the maximum amount which they could possibly realize under the most favorable circumstances if they remained participants in this hypothetical continuing enterprise.

Reference to the facts found by the Commission and both Courts below in this case, and a comparison of this ruling with the lo..g line of earlier decisions denying the

[1] Brief of S. E. C. in Second Circuit Court of Appeals in *New York Trust Company* v. *S. E. C.*, *supra*, p. 58.

payment of premiums to senior security holders[1] suggests that the Commission's new fictional doctrine was designed to free the Commission not only of the limitations stemming from the contractual arrangements of the parties, but also of the settled principles found in the "fair and equitable" standard of 11(e) by the Commission and the Courts. The resultant power of the Com-

[1] The Commission first qualified its previous rulings that fairness and equity did not entitle senior security holders to the payment of premiums in *American Power & Light Company*, Holding Company Act Release No. 6176 (1945). In a vigorous and cogent dissenting opinion Commissioner Healy sharply challenged the Commission's assertion that its previous rulings were "distinguishable" on the ground that in the earlier cases "no attempt was made * * * to establish that the debenture holders' interest in the companies as continuing enterprises were worth more than the face amount of their claim". In point of fact, in virtually all the earlier cases the security holders both before the Commission [see, e.g., *United Light & Power Co., supra,* p. 54] and the courts [see, e.g., *Re Consolidated Elec. & Gas Co.*, 55 F. Supp. 211 at 215 (D. Del., 1944); *In re Standard Gas & Elec. Co.*, 151 F. 2d 326, 332 (C. C. A. 3, 1945), *cert. den.* 327 U. S. 796] had advanced precisely the same contention with respect to the value on "a going-concern basis" of the investments which they were required to relinquish, and had requested compensation for that alleged value.

The only other occasion prior to the instant case in which the Commission required premiums to be paid to the preferred stockholders was in *United Light-American Light & Traction Company*, Holding Company Act Release No. 6603 (1946), in a 3 to 2 decision; thereafter a motion for reargument was granted and decision was reserved for more than a year. While the decision was thus still pending, the company sought and obtained the Commission's approval to remain in business and to embark on a large new venture. The company thereupon made a voluntary proposal to purchase shares of its non-callable preferred stocks with funds obtained through sale of serial notes carrying a much lower rate of interest. (*United Light-American Light & Traction Co.*, Holding Company Act Release No. 7951 [1947].)

The *American Power & Light* decision, *supra*, was thus the only consummated decision prior to that of Engineers in which the Commission applied its new "investment value ex the Act" doctrine. That decision was not contested in the Courts because, as the president of the company pointed out to the stockholders in the annual report, a paradoxical tax situation arising out of the excess tax provisions then in force made it financially advantageous for the company to

mission to function wholly free of restraints and standards calls to mind Jeremy Bentham's pungent characterization of legal fictions:

> "A fiction of law may be defined—a wilful falsehood, having for its object the stealing legislative power, by and for hands which could not, or durst not, openly claim it—and, but for the delusion thus produced, could not exercise it." [1]

The vice in the Commission's fictional assumption that "the enterprise continues" is not merely in its perversion of the facts here, but in its perversion of established doctrine and the principles laid down by this Court in the *Otis* case. We believe that those principles require the application in this case of "the touchstone of the 'fair and equitable' standard": the terms of the contract must prevail. But if those terms are deemed inapplicable, then the rationale of the *Otis* case certainly does not justify the abrupt rejection of the principle of "frustration". On the contrary, this Court held in that case that "fairness and equity" permitted the preferred stockholders to receive the "equitable equivalent" of their claim on earnings because they remained investors in a continuing enterprise; but as the reference in *Otis* (at p. 638) to

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pay the premiums. Consequently, the instant case was the first one in which the Courts were called upon to reverse the long line of non-premium decisions in favor of the Commission's "investment value ex the Act" doctrine, which was and is totally devoid of any judicial support.

Subsequent to its decision in the instant case, the Commission issued one additional decision in which it applied its "investment ex the Act" doctrine (*Pennsylvania Edison Company*, Holding Company Act Release No. 8550, Oct. 15, 1948). That decision, which has not yet been passed on by the Courts, involved a very different fact situation from the Engineers liquidation (*infra*, p. 115, n. 1).

[1] Bentham, A Fragment on Government (Historical Preface to the Second Ed.) 1 Bowring, Bentham Works (1843) 243.

New York Trust Co. v. *Securities and Exchange Commission,* 131 F. 2d 274 (C. C. A. 2), *cert. den.* 318 U. S. 786; and *In re Laclede Gas Light Co.,* 57 F. Supp. 997, makes plain, "fairness and equity" did not permit the debenture holders, whose investment in the same company was being "liquidated" by cash payment, to receive a "windfall" in the form of premium payments to which their contract did not entitle them. The Act of the sovereign in frustrating the contract between the senior and junior security holders did not give the former the right to demand or receive added compensation because the investment they were giving up was highly profitable,[1] any more than the junior security holders could be compensated for their reciprocal deprivation of the continued use of the senior security holders' capital. Here, there is not only "no contractual obligation * * * to pay a redemption premium", but the corporate charter explicitly precludes such payment. In these circumstances, even more plainly

[1] It may be observed that the "investment values" of many of the senior securities covered by the decisions referred to above were substantially equal or superior to those of the Engineers' preferreds on the basis of the usual criteria of earnings and assets coverage, market history and dividend or interest record. In the case of the debentures of United Light, for example, bond interest had been regularly earned and paid (as compared to the failure of Engineers to earn or pay dividends on the preferreds for a period of several years). It may further be noted the Commission stated that the market prices of the debentures of United Light in the period 1940-1942 "had been close to and sometimes as much as 1½ points above par" (10 S. E. C. 1227), whereas during those same years the preferreds of Engineers sold as low as $40-$45 per share (Engineers Exs. 26, 27, 28, R. 1391a, 1392a, 1393a). The notes and debentures of Standard held not entitled to premiums *In re Standard Gas & Electric Co.,* 151 F. 2d 326, 332 (C. C. A. 3, 1945) were so well secured that Standard was able to replace them with *bank loans* bearing interest of only 2½% (see *Standard Gas & Electric Co.,* Holding Company Act Release No. 6345 [1946]).

than in that case "no such obligation * * * exists by virtue of any other recognized legal or equitable principle" (*United Light & Power Co.*, 10 S. E. C. 1215, 1223).

III. Construing the Act as the Commission has construed it—to authorize disregard of applicable charter provisions and well-established legal and equitable principles—would raise serious constitutional questions.

If the Commission is upheld either in its assertion that the "fair and equitable" standard authorized it to regard the applicable charter liquidation provisions here present as not "conclusive", or in its attempt in this case to excise the frustration doctrine from the "fair and equitable" standard, pressing constitutional objections arise.

While Congress unquestionably may cut across or sever contractual obligations in an appropriate exercise of its power to regulate commerce, such interference with freely made agreements must be appropriate, if not necessary, to the enforcement of a clearly defined public policy (*Treigle* v. *Acme Homestead Ass'n*, 297 U. S. 189; *Louisville Bank* v. *Radford*, 295 U. S. 555). If, as the Commission contends, the "fair and equitable" standard is not to be given its traditional meaning as a term of art in this statute, we are faced not only with a plainly inappropriate and unnecessary interference with the contract rights of the parties (cf. Stone, C. J., dissenting in *Otis & Co.* v. *S. E. C.*, 323 U. S. 624, 648-649), but with a delegation of power to the Commission to alter contractual rights without any standard being furnished to

guide the exercise of that power (cf. *Panama Refining Co.* v. *Ryan*, 293 U. S. 388; *Schechter Corp.* v. *United States*, 295 U. S. 495).

In the first place, as we have shown the Commission's direction to pay premiums to Engineers' preferred stockholders is a command which the Commission in a long series of judicially approved rulings has indicated the "fair and equitable" standard does not authorize it to make. One may assume *arguendo* that the Commission was not rigidly bound by the doctrine of *stare decisis*, or by its own consistent administrative interpretations [1] of the "fair and equitable" standard for which over a four-year period it had repeatedly asked and unfailingly received full judicial approval. But, plainly, a delegation of power which would authorize such flatly contradictory results would not furnish that guidance which it has never been doubted Congress must furnish to administrative agencies to which it delegates powers to regulate the affairs of citizens (cf. *Panama Refining Co.* v. *Ryan*; *Schechter Corp.* v. *United States*, *supra*).

In the second place, if the historic command of the "fair and equitable" standard—that contractual rights must be enforced—is no longer binding, it is impossible to ascertain what that term means. The unconstitutional ambiguity of the "fair and equitable" standard, if that standard does not have its historically developed meaning, is demonstrated by an examination of the Commission's action in this case. Thus, a primary consideration upon

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[1] With respect to the weight attributed to consistent administrative interpretation, see *U. S.* v. *American Trucking Associations*, 310 U. S. 534, 549; *Federal Trade Commission* v. *Bunte Bros.*, 312 U. S. 349.

which the Commission rested its valuation of the preferred stock here is the dividend rate to which the preferred was entitled by Engineers' charter, and the hypothetical "value" allegedly accorded thereto by the market (see infra, pp. 74 *et seq.*). But if, as the Commission claims, it had the authority to refuse to be bound by the liquidation provisions of Engineers' charter, and in fact, as is plain, it gave absolutely no consideration to the contractual mandate,[1] by virtue of what criterion does any other provision of the charter become entitled to the controlling significance which the Commission here gave the dividend rate?

The dividend rate constituted merely one provision of an integral contract between the stockholders. The obligation of the common stockholders to pay the stipulated dividend rate was inextricably interrelated with the numerous other contractual provisions such as those dealing with conversion, redemption, liquidation, right to issue additional preferred on a *pari passu* basis, etc. It is axiomatic that all these provisions are related to and interwoven with the dividend rate, and all interact upon one another.[2]

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[1] Compare p. 44, n. 1, *supra*.

[2] See, e.g., McDiarmid, "The Utilities Face A Big Financial Problem" (Public Utilities Fornightly, Jan. 1, 1948, pp. 8-9):

> "There is a fairly good chance that utilities might reclaim the interest of institutional investors in their preferreds by concessions as to sinking funds or convertibility. * * *
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> * * * It is noteworthy that in recent weeks two utility preferred stock issues, roughly comparable as to quality, were brought out a day or so apart from each other. One was sold on a 4.4 per cent yield basis but was convertible into common. It was an immediate sellout. The other came on a 4.5 per cent yield basis but was not convertible. It was sold slowly and has since dropped in the market seven points below its offering price."

Thus, the inclusion of a charter provision prohibiting subsequent issuance of preferred stock having an equal claim in earnings and assets with that being issued, or other protective provisions of this type (including special provisions on liquidation) will permit the marketing of a preferred bearing a lower dividend rate; while conversely lack of such features must be compensated by a higher dividend rate. It follows that where an effort is made to alter one of these factors, correlative adjustments must be made in many others; if greater rights on liquidation are now given the Engineers' preferred holders, a retroactive adjustment on the high dividend rate paid during past years is clearly in order.

It is thus evident that attempts to tamper with the correlative rights and obligations integrated in the charter contract between the preferred and common stockholders, inevitably entail acute problems not foreseen or mentioned in the Commission's opinion.[1]

If, as it contends, the Commission is left free by the "fair and equitable" standard to assign differing significance to different "portions of the charter" in its own unguided discretion, attributing one meaning to the stand-

[1] The preceding discussion merely touches on a few of these problems. There are others equally acute. For example, if the charter liquidation provisions are nullified, we come face to face with the settled rule of law that a preferred stock has no preference in liquidation. If the charter is silent the preferred holders merely participate pro rata with the common, share for share, and on such a basis the preferred would realize something less than $50 per share in this liquidation. *Continental Insurance Co.* v. *U. S.*, 259 U. S. 156, 181; 11 *Fletcher, Cyc. Corp.*, § 5303, and 16 *Fletcher, supra*, § 8226. Cf. *Holland* v. *Nat'l Automotive*, 22 Del. Ch. 99, 194 A. 124; *Ellingwood* v. *Wolf's Head Oil Refining Co.*, 38 A. 2d 743 (Del. Sup. Ct., 1944).

ard one day and precisely the opposite meaning the next day,[1] respondents submit the delegation of authority is unconstitutional. Before so unbridled a delegation of authority will be imputed to Congress, unmistakable evidence of such an intent must be shown.[2] In this case no such evidence is forthcoming. On the contrary, the legislative history and judicial decisions point to precisely the opposite conclusion.

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[1] It may further be noted that the Commission had in an earlier opinion plainly indicated that the involuntary liquidation preference of the Engineers' preferred stocks represented "the maximum claim of the stock", a statement consistent with the Commission's long line of non-premium decisions discussed above. In that decision (Holding Company Act Release No. 4997, April 15, 1944, R. 2128a-2138a) the Commission stated (R. 2135a):

> "* * * we pointed out in relation to the earlier case that as the amount to be received by the preferred stockholders tends to approach *the maximum claim* of the stock, the likelihood of any unfairness would be diminished. As noted above, the current market prices of the three series of preferred stocks which Engineers now proposes to reacquire are close to *the involuntary liquidating prices* and under the circumstances we are satisfied that the proposed reacquisition is not unfair to the security holders of Engineers." (Emphasis supplied.)

It cannot be doubted that many preferred stockholders who decided to sell their stock at that time at prices in the 90s (R. 2134a), as well as common stockholders who decided to retain their holdings, were influenced in their actions by this statement, viewed in the light of the Commission's long and unbroken line of non-premium decisions.

[2] *United States v. Standard Brewing Company*, 251 U. S. 210, 220; *United States v. Bennett*, 232 U. S. 299; *Harriman v. Interstate Commerce Commission*, 211 U. S. 407.

PART TWO

IF THE RIGHTS OF THE STOCKHOLDERS WERE TO BE VIEWED AS "IN A CONTINUING ENTERPRISE", THE COMMISSION'S "INVESTMENT VALUE EX THE ACT" DOCTRINE AS HERE APPLIED WHOLLY FAILED TO MEASURE THE EQUITABLE EQUIVALENTS OF SUCH RIGHTS. THE COMMISSION'S DOCTRINE, MOREOVER, CONTRAVENED THE STRICT PRIORITY PRINCIPLE AND WAS OTHERWISE FALLACIOUS.

IV. The Commission did not in fact evaluate the stockholders' rights or securities on the basis of a continuing enterprise. On such basis, the preferred holders would have been entitled to no more than $100 per share, and probably less.

If, notwithstanding our contentions set forth in the preceding portions of this brief, it be nevertheless concluded that in this liquidation "fairness and equity" permitted rejection both of the charter liquidation provisions and of previously formulated and manifestly apt liquidation standards, and authorized transmutation of the rights of the Engineers' stockholders on "a going concern basis" into "equitable equivalents" as was done in *Otis*, then we contend, and propose now to demonstrate, that the determination made by the Commission failed by a wide measure to satisfy such requirements.

Our contentions may be concisely summarized as follows: (a) the "investment value" for which the Commission found the preferred stockholders were to be compensated was nothing more or less than a transient "value" based wholly on market prices as of a specific haphazard date; (b) the doctrine of "equitable equivalents" which the Commission purported to invoke in measuring the

"compensation" to which the preferred stockholders of Engineers were entitled for their stock does not authorize compensation resting upon such essentially accidental "values"; if compensation were to be awarded in terms of average long range values of the preferred stock, no more than $100 could be found as the "equitable equivalent"; and (c), apart from its erroneous reliance upon a transient market "value", the Commission's application in this case of the doctrine of "equitable equivalents" failed to take account of the correlative rights of the common stockholders, which are an essential ingredient of the doctrine of "equitable equivalents" as enunciated by this Court; upon any proper construction and application of the doctrine of "equitable equivalents", the preferred stockholders are entitled to no more than $100 per share.

A. The so-called "Investment Value" as determined by the Commission represented merely transient market value at a specific moment.

This Court has cogently admonished that "*value is a word of many meanings.*"[1] The term "investment value" as used by the Commission in this case is particularly misleading because it carries the connotation given to that term in *Otis* of representing value of a stable, long range character as distinguished from transient "values" or prices which fluctuate from day to day with the vagaries of the market place. But it is precisely the latter type of "value" and not the former, to which the Commission here applied the euphemistic title of "investment value".

It will be noted that the Commission's opinion did not at any point define "investment value" and actually em-

[1] Douglas, J., in *Group of Investors* v. *Milwaukee R. R.*, 318 U. S. 523, 540, quoting Mr. Justice Brandeis.

ployed the term in a variety of verbal combinations. However, in spite of the Commission's indiscriminate use of the varying terms "investment value" (R. 67a), "present investment value" (R. 66a), "fair investment value on a going-concern basis" (R. 67a), and "investment worth on a going-concern and apart from the Act, under prevailing yields applied to comparable securities" (R. 67a), the record makes clear beyond any doubt that the only "value" which the Commission determined was a hypothetical market value of the preferreds based on market prices as of the time when the testimony of Badger and Barnes was given (the first few months of 1946).

That portion of the Commission's opinion dealing with the "value" of the preferred stocks is confined to some six pages (R. 62a-68a) of its sixty-page opinion of December 4, 1946 (R. 25a-85a). After setting forth without comment some statistical material (R. 62a-65a), the Commission turned to a brief discussion of the report of Badger, a witness on behalf of certain preferred stockholders. Summarizing in a few short paragraphs certain of Badger's findings (R. 65a-66a), the Commission stated that Badger's conclusions were not seriously "challenged", and were in fact substantially admitted by the company's president, Barnes,[1] as well as in the company's

[1] Although the Commission's opinion states that "Company witnesses several times testified to the same effect" (R. 67a) Barnes was the only witness on behalf of the company who testified in any way on the subject of values or who discussed Badger's testimony. The testimony of Barnes, who was formally qualified as a valuation expert (R. 1138a), is discussed, *infra*, p. 82. One other company official, Benjamin, merely stated that he agreed with Barnes' statement that the company would have taken advantage of the low money rates by "refunding" the preferred stocks at lower dividend rates, if the Act had not required the company's dissolution and the retirement of the preferreds (R. 965a).

brief. It thereupon reached its conclusory finding: "it is apparent that the preferred has an investment value at least equal to the respective call prices" (R. 67a), a statement which necessarily referred to Badger's conclusions viewed in the light of the alleged admissions of the company.

Badger's evidence consisted of a written report and oral testimony with respect to it.[1] Succinctly stated, Badger's technique for evaluating the preferred stocks consisted in selecting a group of allegedly comparable utility preferred stocks, computing their yields (i.e., the ratio of their dividend rates to their market prices) as of the week ended January 4, 1946, and by applying a similar "yield" to the preferred stocks of Engineers arriving at what was variously termed "their present investment values on a going-concern basis", "fair investment value", or merely "investment value".

Although in the earlier sections of Badger's report there is to be found some analysis of so-called "investment characteristics" of the Engineers' preferreds such as asset and earning coverage (R. 2066a-2076a), it is important to note that this "analysis" did not constitute the basis for Badger's ultimate conclusion respecting "values". Those investment characteristics established, as Badger conceded, that on the basis of intrinsic merit the Engineers' preferreds were of inferior caliber, termed by

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[1] Badger's report is set forth at pp. 2057a-2086a of the Record as Preferred Stockholders' Exhibit No. 29. During cross-examination he admitted certain errors and upon his request was given leave to file an amended report (Preferred Stockholders' Exhibit No. 29A, R. 2087a). For Badger's direct testimony, see R. 1009a-1039a; for cross-examination, R. 1040-1189a, Redirect and Recross, 1189a-1205a.

Badger "medium grade".[1] But the purpose for which these investment characteristics were employed by Badger was merely to afford a basis for the selection of allegedly "comparable" securities in order to determine the market prices and yields (i.e., the ratio of dividend rate to market price) at which those securities were selling at that particular moment.[2] Both comparative charts expressly state that "current prices" and "yield" figures were computed on the market prices for the week ending January 4, 1946.[3]

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[1] Badger's admission that on the basis of intrinsic quality the Engineers' preferreds were not high grade is stated somewhat obliquely as follows (R. 2079a): "The preferred stock of Engineers Public Service Company as well as the preferred stocks of the five public utility holding companies studied for comparative purposes, *must be classed as medium grade preferred stocks,* and should, therefore, sell at yields higher than the yields registered by the high grade preferred stocks." See also specific admission under cross-examination (R. 1133a), and compare Barnes' emphatically expressed view that the Engineers' preferreds were "closer to a common stock or a low grade preferred" (R. 1138a, 1140a).

[2] It may be noted that the preferred stocks employed by Badger for "comparative" purposes were proven in fact not to have been appropriate for such purpose, since all of them had investment characteristics superior to those of the Engineers' preferreds and had been accorded superior investment ratings by the recognized independent investment analysts (cf. Engineers' Exhs. 73, 77, R. 1844a, 1850a-1851a). Moreover, in addition to a list of five holding company preferreds of superior quality as aforesaid, Badger also employed a list of 9 *operating* company preferred stocks (R. 2081a) which are necessarily of superior quality to those of a holding company preferred stock such as Engineers, in view of the fact that they are not preceded by the preferred stock of operating companies and are junior to a smaller amount of senior securities. The company sharply challenged the comparability of these securities (Exhibits and testimony, *supra*); but the Commission did not pass on this issue, presumably since it rested upon the alleged "admission" of Barnes and the company hereinafter discussed.

[3] See Preferred Stockholders' Ex. No. 29, table at R. 2077a (next to last item termed "Current Market, Week Jan. 4, 1946)"; see also table at 2081a, footnote 1 "Unless otherwise marked, prices are average sale for week ending January 4, 1946 as per Commercial & Financial Chronicle".

Badger made no reference to the prices at which these same securities had sold in previous weeks or previous years; he did not suggest that it would be appropriate to employ some sort of median prices and yields computed on the basis of prices covering a representative period of time.[1] Instead he used the prices and yields for the week ending January 4, 1946, without modification or adjustment of any kind; and with respect to the level at which those prices and yields stood, he stated:

> "* * * yields on preferred stocks are at the present time, the lowest which they have ever been in the history of our country, or conversely, * * * the prices of such stocks are at the highest levels ever experienced. The permanency of this situation will depend on the permanency of low interest rates" (R. 2065a).

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[1] The following table shows the range of prices, during the preceding five years, of three of the five holding company preferred stocks used by Badger for comparative purposes (Moody's, Public Utilities, 1946, p. a66 et seq.) as compared with the prices used by Badger (R. 2077a) in computing their yields:

	Columbia Gas & Electric Moody's, *supra*, p. a69		*Pacific Public Service* Moody's, *supra*, p. a78		*Public Service of New Jersey* Moody's, *supra*, p. a79	
	High	*Low*	*High*	*Low*	*High*	*Low*
45	107½	84	27⅜	22¾	115¾	102⅝
44	93	70	23½	19	103⅞	87½
43	73	37	19¼	14⅛	96¼	75½
42	45½	29	14¼	11¾	86⅜	62
41	72	42⅛	18⅜	10⅛	110	75¾
dger (R. 2077a)	105.50		26.50		114.38	

The other two holding company preferreds employed by Badger display a range of prices similar to those shown above (Moody's, *supra*, p. a76, p. a83); but see Badger's note (R. 2077a) as to the deductions which must be made for dividend arrears on the Niagara Hudson Power Preferred. The average yield of all five stocks for the five-year period 1941-1945, computed on their mean price during each year, was 6.3%. Badger used a yield of 4.6% (R. 2111a).

Far from being troubled by the fact that the market prices he was proposing to use were at "the highest levels ever experienced" and preferred yields at "the lowest * * * in the history of our country", Badger went on to express the positive view that such values were "permanent", because they were "predicated on fundamental conditions prevailing in the money markets, conditions which are of a permanent nature" (R. 2066a). Although conceding that the unprecedentedly low money rates were primarily due to the pegging of the Government bond market (R. 1060a), the only possibility of any change in money rates and preferred yields that Badger was willing to envisage was the probability that they would go still lower (R. 1085a-1086a).

Some months after Badger's testimony was given, the Government lowered the support levels at which Government securities had been "pegged", causing the start of the rise in interest rates which has been in progress ever since; and at about the same time stock market prices began to decline. The fall in prices of public utility stocks which then ensued, and thereafter continued, was much sharper than in the case of industrial stocks,[1] due to the fears of investors that the impact on the utility industry of the alternative threats of inflation and deflation might be especially severe, as had been the case following termination of the First World War. Reflecting both this

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[1]

	Federal Reserve Index of Industrial Stocks	*Federal Reserve Index of Public Utility Stocks*
March 1946*	145	123
Oct. 30, 1948**	137	98
% Decline	5½%	20%

* Federal Reserve Bulletin, June, 1946, p. 642

** Federal Reserve Bulletin, November, 1948, p. 1396

adverse outlook and the increase in money rates, the decline in prices and the increase in yields has been particularly great in the case of utility holding company preferred stocks, which are necessarily much more speculative than the preferred stocks of operating companies.[1]

Except for Badger's naked statements of opinion as to the "values" of the Engineers' preferreds and the "permanence" of the then current money rates and yields, the record is entirely barren of any evidence on which the Commission could have based a judgment or finding that the "values" for the Engineers' preferred as found by Badger were of a long range character.[2]

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[1] For express recognition by the Commission of the substantial increases in public utility holding company preferred yields and declines in market prices which have taken place since the time of Badger's testimony, see quotation from the Commission's opinion in *American Light & Traction-United Light Co., supra*, p. 12, n. 1.

See also p. 95, n. 2, *infra*, for specific figures measuring the extent of the decline.

[2] Any suggestion that the Commission might have given weight *sub silentio* to factors other than the Badger and Barnes testimony discussed in its opinion, is not only negatived by the Commission's own statement that this investment value "is apparent" from the testimony which it had just discussed, but also by examination of the few other factors mentioned, *without comment* in that portion of the Commission's opinion dealing with the value of the preferreds. Only five items will be found there (R. 62a-65a):

1. A statement with respect to the dates and prices at which the preferreds were originally issued. (Cf. District Court Findings 22-23, R. 301a.)

2. Reference to the dividend history, including the fact that dividends were in arrears during a four-year period.

3. A summary of the market history of the preferreds establishing that their market price over the entire period they were outstanding was between $63-$67 per share.

4. A capitalization table establishing that on a consolidated basis common stock and surplus equalled only 16.3%, and that the preferred stock was *junior* to 66.2% of system capitalization. The Commission's failure to comment on these figures must be considered in

If the Commission in accepting Badger's conclusions as to the "investment value" of the Engineers' preferreds rested upon his judgment as to the "permanence" of those values and the money rates on which they were predicated, then it is evident that the Commission's determination stands exposed as having been no less erroneous than Badger's judgment. Even if Badger's bare statements in this respect (which were challenged and discredited by company witnesses and counsel, see *infra*, pp. 81-82) could be said to constitute "substantial evidence" to support his conclusion, the District Court,

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light of the fact that the Commission has repeatedly stated that it regards 25% as the minimum acceptable ratio of common stock capitalization, and a 50% ratio of senior capitalization (prior to preferred stock) as the maximum. (See *Interstate Power Company*, Holding Company Act Release No. 7143, p. 18; *Western Light & Telephone Co.*, Holding Company Act Release No. 5902; cf. 13th Annual Report of S. E. C., pp. 88-90.)

5. Two tables (R. 64a-65a) establishing that for the period 1937-1945 Fixed Charges and Preferred Dividends on a consolidated basis were covered by the extremely slim margin of 1.3 times. Moreover, no explanation is offered as to why this table stops with the year 1937. During the three years immediately preceding, "Fixed Charges and Preferred Dividends" were on the average not covered even once (R. 1433a, 1443a, 1461a; cf. Moody's Public Utilities, 1940, p. 1314).

Clearly the foregoing items all point in the direction of a value of less than $100 for the preferreds, and therefore cannot be deemed to have afforded a basis for the Commission's determination that the premiums should be paid.

Nor can the use by the Commission of the customary omnibus phrase "upon a full consideration of the entire record" (R. 68a) serve to bestow immunity on its finding. As has been shown, the record is barren of evidence to support the finding other than the Badger and Barnes testimony herein discussed. The use of this type of "talismanic phrase" (*City of Yonkers* v. *U. S.*, 320 U. S. 685, 698) cannot circumvent this Court's admonition that "The grounds upon which an administrative order must be judged are those upon which the record discloses that its action was based" (*S. E. C.* v. *Chenery Corp.*, 318 U. S. 80, 87); Cf. Section 8(b) of The Administrative Procedure Act (5 U. S. C. 1008(b)).

having perceived and pointed out this error,[1] could not, under any view of its duties, enter its decree approving and enforcing the plan.[2]

But if the Commission did not accept Badger's views as to the permanence of the "values" set forth in his report and testimony, then it follows that the Commission merely accepted Badger's conclusions that the Engineers' preferreds had a value approximating the redemption prices based exclusively on market prices as of January 4, 1946 ("the highest they have ever been in the history of our country") and without regard to whether or how much those prices and values might decline in subsequent weeks, months or years. This would mean that not only did the Commission deem irrelevant in determining "investment value on a going concern basis" the entire past history of these stocks on a going concern basis which established an average market price of $63-$67 per share (R. 62a) but it also deemed equally irrelevant their future course if permitted to remain outstanding as part of a continuing enterprise.

That this was indeed the Commission's view is attested by its statement that "no serious challenge was made in the proceeding to Badger's conclusion that 'the fair investment value of the preferreds on a going concern basis'" approximated the redemption prices, and its refer-

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[1] District Court Findings 52-54, R. 314a-315a.

[2] The decree of a court of equity speaks "as of the date of entry" and therefore must take into account all material changes which have occurred since the commencement of the proceedings: *Randel* v. *Brown*, 2 How. 405, 422; *McCabe* v. *Guaranty Trust Co.*, 243 F. 845, 849; *Brooks Bros.* v. *Brooks Clothing of California*, 60 F. Supp. 442, 456. Cf. *Knight* v. *Wertheim & Co.*, 158 F. 2d 838 (C. C. A. 2), *cert. den. sub. nom. McGuire* v. *Equitable Office Building Corp.*, 331 U. S. 818.

ence to the statements of Barnes and the company's counsel in substantiation (R. 67a). For while Barnes and the company counsel agreed "if there were no Holding Company Act or the Act were repealed today" (R. 67a) so that Engineers were not required to go out of business, the preferreds would momentarily have sold at about the redemption prices because of the extremely low money rates, they affirmed time and again with all possible vigor that the unprecedentedly low money rates then current ~~were~~ primarily the result of the Government's "pegging" policies which might be revised at any time (R. 1056a-1060a, 1087a, 1136a-1146a); that the then current market prices also reflected the fact that "we are in a boom period at this time" (R. 667a); that the redemption prices could by no means be considered "a fair value which will be maintained as an average for an indefinite period of time" (R. 522a); that the Engineers' preferred stock if permitted to remain outstanding could not rise higher than the redemption prices, and would be confronted by many adverse factors (discussed with particularity) which would inevitably result in price decreases which the past market history showed were likely to be very great (R. 523a-525a).[1]

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[1] The Company's Brief to which the Commission's opinion refers is not part of this record, but the oral argument of company counsel before the Commission contains almost verbatim quotations from that brief and establishes that the following was stated by Engineer's Counsel with reference to the "investment value" of the preferreds (R. 1219a):

> "* * * I would like to point out the inequity of placing much emphasis on the so-called present investment value of the preferred stock, ex the Act. That investment value has no such permanence as to entitle it to any considerable weight. Market values are the resultant of two variables—(1) the cost of money, and (2) the risk factor determined largely from earnings. A holding company preferred stock, although a fixed income stock,

Since the Commission's finding that "it is apparent that the preferred stock has an investment value at least equal to the respective call prices" (R. 67a) rests upon the agreement which it found between Badger's evidence and the alleged admissions of Barnes and the company's counsel as to the validity of Badger's conclusions, it is plain that the Commission's findings went no further than these admissions. Consequently, it follows that contrary to petitioners' contention that the Commission evaluated "the rights of stockholders * * * on the basis of a going business and not as though a liquidation were taking place",[1] what the Commission *actually* did was to "value" the preferred stocks alone merely on the basis of market prices prevailing in January-May, 1946, "the highest in the history of our country".

Both the District Court and the Court of Appeals so found.[2] And the District Court, after pointing to various

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by its very nature is inherently about the most volatile fixed income security in the market. Dr. Badger's claim in his testimony that present market values of preferred stocks are 'as far as one can humanly predict, a permanent level' is extravagant and unrealistic.

Holding company preferred stocks are at the moment close to their all-time peak and under the circumstances of this case, since the premiums are a ceiling on the market values, the values of those preferred stocks have only one way to go and that is downward; and that they will go down and go down considerably, is inevitable. That result is only a matter of time; and it may be soon * * *."

[1] See Commission's Petition for Certiorari (No. 226), p. 14.

[2] District Court Findings 41-54, R. 310a-315a; Cf. Court of Appeals Opinion (R. 17): "We think it is apparent *on a careful examination* of the testimony of the two men that each was testifying to values as of May 1946, ex the Act". (Emphasis supplied.)

other arbitrary and inequitable assumptions by Badger and the Commission (R. 310a-312a),[1] stated:

> "The extremely low money rates which resulted in Badger's finding that the preferred stocks of Engineers have an 'investment value' greater than $100 per share, largely reflect artificial factors which are clearly subject to changes at any time and may well be of purely transitory character" (R. 314a).

After carefully noting the changes in market prices and yields which had taken place since Badger's testimony, and which showed how mistaken were his notions as to "permanence",[2] the District Court posed this cogent question which, we submit, pierces to the heart of the Commission's fallacious valuation:

> "Assuming the correctness of Badger's estimates of the investment values of the Engineers' preferred stock 'on a going concern basis', subject to all the infirmities above referred to, the question still is: '*investment values' for how long?*" (Emphasis supplied.)[3]

Pointing to the fact that the record indicated "that there are other imponderables and variables, aside from the trend of money rates alone, which might affect the future

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[1] Thus, the District Court pointed out (R. 310a-312a) that in arriving at these theoretical values allegedly "*ex* the Act" based on the then current market prices, neither Badger nor the Commission made any adjustments whatever for the important values attributable directly to the impact of liquidation; accordingly they appropriated for the benefit of the preferred stocks in thus evaluating them, the sums belonging to the common stockholders which had been laid aside specifically for the purpose of carrying out the statutory mandate to retire the preferred stocks and to liquidate (R. 470a, 578a; Engineers' Ex. 30, R. 1395a).

[2] Finding No. 52, R. 314a.

[3] R. 312a, Finding No. 48.

'investment value' of the Engineers' preferreds, measured on the theoretical going-concern basis" (R. 315a), the Court concluded:

> "The record establishes that the investment values of the Engineers preferred stocks found by Badger at the time of his testimony do not represent the investment value of these stocks in the past, and are by no means determinative of the investment value of these stocks for any considerable period of time in the future. Because the preferreds' redemption provision acts as a 'stopper', the future investment value cannot become greater than the call price, but on the other hand may very well become much less. *The record further establishes that there are present many factors of a potentially adverse character*, and that the extent to which the investment value of preferred stocks of this character can decline under adverse conditions is indeed very great" (R. 315a). (Emphasis supplied.)

The District Court thus clearly recognized that two elements, in interaction, would determine the normal, long-range value of the preferred stocks if they remained outstanding as part of a going concern: (1) the future course of earnings of the operating companies, under the impact of foreseeable economic developments; and (2) the future course of money rates applicable to holding company preferred stocks of this caliber. As we have shown, to neither of these factors did the Commission accord even the slightest consideration, notwithstanding the emphatic warnings of the company witnesses and representatives that the exceptionally high earnings and low money rates of that moment rested heavily upon temporary artificial factors incident to post-war economic and financial phenomena. Thus, while insisting that valua-

tion of stockholders' rights must be predicated on the assumption that "the enterprise continues", the Commission determined the "value" of the preferred as though economic conditions, money rates and the enterprise itself were all permanently frozen in their course as of January, 1946—a period which the Commission has itself termed "the peak of the war-time market".[1]

B. The doctrine of equitable equivalents does not permit the use of a momentary market price to measure the "rights" of the preferred stockholders. On any other than a transient basis, the Engineers' preferreds could not be valued at more than $100.

(1) It is scarcely open to question that transient values predicated on the market prices of securities as of a particular haphazard moment cannot be accepted as the measurement of their intrinsic worth, or as the appropriate standard for determining "fairness and equity" or "equitable equivalence" in reorganizations or liquidations.

It is fundamental that in valuation for reorganization purposes earning power and other relevant economic factors must be calculated *prospectively* on a normal going-concern basis, with due regard for the record of the past.[2]

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[1] Actually, the liquidation of Engineers did not take place until almost a year and a half later, July 21, 1947 (Moody's Public Utilities, 1948, p. 403) and the retirement of the preferred stocks until June 30, 1947.

[2] Cf. *Consolidated Rock Products Co.* v. *Dubois*, 312 U. S. 510, 526: "Since its application requires a prediction as to what will occur in the future, an estimate, as distinguished from mathematical certitude, is all that can be made. But that estimate must be based on an informed judgment *which embraces all facts relevant to future earning capacity* and hence to present worth, including, of course, the nature and condition of the properties, *the past earnings record*, and all circumstances which indicate whether or not that record is a reliable criterion *of future performance*." (Emphasis supplied.)
Cf. *Group of Investors* v. *Milwaukee R. Co.*, 318 U. S. 523, 565-6.

Consistently with that principle, the term "investment value," as employed by this Court in its *Otis* decision had reference to the values on a long-range basis of both classes of stockholders predicated upon their relative rights to participate in the prospective earnings of the enterprise. Thus, as this Court pointed out, the common stockholders' right to participate in the estimated earnings commencing some fourteen years in the future, established the "investment value" of the common which entitled it to an allocation of approximately 5% of the assets of the company being dissolved. In turn, the preferreds' right to receive all of the prospective earnings for a fourteen-year period until the arrearages of dividends had been eliminated, and a lesser portion of such earnings thereafter, established its right to an allocation of 95% of the assets. It is therefore plain that reliance on market prices as the standard for determining "investment values" on a going-concern basis is both foreign and repugnant to the *Otis* doctrine, which emphasized the traditional reorganization criteria of compensating surrendered rights in terms of prospective earning power.[1]

The Commission has itself stated many times that market values cannot be accepted as a criterion for determining values or measuring equitable equivalents in connection with Section 11(e) plans. Thus, in *Washington Railway and Electric Company*, Holding Company Act Release No. 7410 (May, 1947), the Commission stated (p. 27):

[1] *Otis & Co. v. S. E. C.*, 323 U. S. 624, 631-633. Cf. also detailed analysis of the valuation technique employed in *Otis* in Circuit Court opinion, *In re Securities and Exchange Comm. (Otis & Co.)*, 142 F. 2d 411, 420-421.

"However, we have never considered market values as determinative of the fairness of a section 11(e) plan and it is therefore unnecessary for us to make an estimate of the market value either of the presently outstanding preferred stock apart from the possibility of liquidation or of the package of securities which the preferred stock is to receive under the proposed plan."

These words were directed squarely to the question of the standards applicable to evaluating on a "going concern" basis the rights of the preferred stockholders whose stock was being retired in a liquidation compelled by Section 11, only a few months following the Commission's decision in the instant case. The only difference is that the Commission in that decision, as well as in the many others where similar statements are made,[1] did not

[1] Thus, in *Northern States Power Co.*, Holding Company Act Release No. 7950 (1948), approved and enforced 80 F. Supp. 193 (N. D. Minn., 1948), the Commission stated in its brief in the District Court (p. 25):

"* * * current market price earnings ratios, no matter how applied, are normally irrelevant to the question of reorganization values. If it were possible to determine mathematically, on the basis of present markets, that the market value of a given number of shares of Minnesota Company common stock is exactly equivalent to the liquidation preference of the Delaware preferred stock, the equation would immediately be upset as soon as the market would go appreciably up or down. As pointed out by the Commission, to the extent that capitalization rates are important at all, *the pertinent rate to be considered is one appropriate over the long run rather than one based on the market at any given moment.*" (Emphasis supplied.)

In *Community Gas and Power Company*, Holding Company Act Release No. 7131 (January 15, 1947), the Commission replied as follows to the contention of secured debenture holders of a holding company being liquidated (p. 20):

"In effect, their argument is that the market price on the day of distribution of the securities allocated to them is the conclusive measure of their participation and that they are entitled

use the "present investment value ex the Act" doctrine which it applied in the Engineers' case and which, it has elsewhere conceded, would make hypothetical current market prices of the senior securities "apart from liquidation" the paramount criterion in determining fairness and equity.[1]

If market values were deemed the paramount criterion for determining whether senior security holders have received the equitable equivalent of their claims in liquidations or reorganizations under Section 11(e), the Commission and the courts could hardly have found "fair and equitable" the various plans carried out as recently as during the past eighteen months. Thus the holders of the 6% debentures of Community Gas and Power Company, having a secured and well-covered claim of $1214 per debenture ($1,000 principal amount plus $214 accrued interest), received in the liquidation of the holding company 87 shares of Minneapolis Gas Light common stock, of which the current cash value at date of distribution

to receive securities with a current market value, equal to the face amount of their claim. *With that we cannot agree.*" (Emphasis supplied.)

See discussion in the text on this page of the "equitable equivalents" which these bondholders received. The plan was enforced in the Courts, and this Court denied certiorari: *Community Gas and Power*, 71 F. Supp. 171 (D. Del., 1947); aff'd 168 F. 2d 740 (C. C. A. 3); *cert. den., sub nom. Vanneck* v. *S. E. C.*, 334 U. S. 846.

[1] See quotation from the Commission's opinion in *United Light and Railways Co.-American Light & Traction Co., supra*, p. 12, n. 1, where the Commission stated: "It is apparent that insofar as *investment value is derived from an analysis of the current yields* of comparable securities, the investment value of American's preferred has been substantially affected in the interim." (Emphasis supplied.) As has previously been pointed out, "yields" are computed on the basis of the *market prices* at which the securities are selling as of the time the computation is made, and such "yields" fluctuate directly with the fluctuations in the market prices.

aggregated $1000.[1] The holders of 7% preferred stock of Northern States Power Company of Delaware, having a claim of $110 per share (entitled on redemption to $120), amply covered by assets, received in liquidation of the holding company 10 shares of Northern States of Minnesota common stock and $3.50 in cash, having a total cash value on date of distribution aggregating $88.50.[2] The holders of 6% preferred stock of Wisconsin Hydro Electric Power Co. for their claim of $176.50 received operating company common stock having a cash value of approximately $100.[3] The holders of 7% Prior Lien Preferred stock of North West Utilities Company for their claim of $203 (entitled on redemption to $213) received common stock having a cash value of $165.[4]

In all the foregoing decisions, which are typical, the Commission reached these results by insisting that market values as of the time of liquidation were not significant and that the determining factor was the earnings' claims of the security holders measured against the future earn-

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[1] *Community Gas & Power Company*, Holding Company Act Release No. 7131 (1947); approved and enforced, 71 F. Supp. 171 (D. Del.); aff'd 168 F. 2d 740 (C. C. A. 3), *cert. den.* 334 U. S. 846. Market value of *Minneapolis Gas Light* common as of approximate date of distribution, Wall Street Journal, 8/31/48.

[2] *Northern States Power Company*, Holding Company Act Release No. 7950 (1947); approved and enforced 80 F. Supp. 193 (No. Dist. Minn.). Market value of *Northern States of Minnesota* common as of approximate date of distribution, National Daily Quotation Service, Oct. 7, 1948.

[3] *Eastern Minnesota Power Company*, Holding Company Act Release No. 7822 (1946). Price of common stock as of approximate distribution date, National Daily Quotation Service, Jan. 6, 1948.

[4] *Middle West Corporation*, Holding Company Act Release No. 7905 (1947); approved and enforced; *North West Utilities Co.*, 76 F. Supp. 63 (D. Del.).

Price of *Wisconsin Power & Light* common stock as of approximate distribution date, National Daily Quotation Service, March 5, 1948.

ing power of the assets to be distributed among the security holders. In each of these cases application of the "investment value ex the Act" formula as here applied would have required payment to the preferred holders of amounts in excess of their liquidation claims, but the Commission rejected such market value criteria as irrelevant ~~and~~ inapplicable. Yet in the instant case the Commission reached its result by insisting that current market value was of controlling significance, and wholly ignoring apportionment of future earning power in evaluating the equitable equivalent of the rights surrendered by both classes of stockholders.

Confronted with the foregoing, Commission Counsel find it necessary to execute a sharp *volte face*. After having stated that the Commission justifies its decision in the instant case on the *Otis* principle which required the rights of security holders to be evaluated on the basis of a going business and not as though a liquidation were taking place,[1] they now assert, in effect, that the Commission was entitled completely to ignore the rights of the security holders on a going-concern basis because, here, liquidation rather than reorganization is taking place and the *Otis* principle is for that reason inapplicable. Thus they state.[2]

> "The court below criticized the Commission for failure to ascertain the future earning power of the system and to apportion that earning power between the preferreds and common based on their respective claims to income 'as it did in the United Power & Light case' (R. 35). But that technique is appropriate only where, as under the United Light & Power

[1] Commission Petition (No. 226), p. 14.
[2] *Id.*, p. 16.

plan, a new security is being allocated between preferred and common stockholders. The plan here involved * * * contemplates *paying off the preferred in cash.*" (Emphasis supplied.)

We freely concede that "paying off the preferred in cash"—$39,000,000 of cash raised in the process of liquidation—is indeed a plain indication that true liquidation and not mere reorganization is occurring, and that the principles applicable to such a liquidation (as discussed, *supra,* and as applied by the District Court) should here prevail. Indeed, that is our major contention in Part I of this Brief. But the Commission cannot have it both ways: it cannot urge that it was justified in ignoring liquidation principles and evaluating rights on the "basis of a going business" as in *Otis,* and at the same time argue that evaluation of rights on the basis of a going business as in *Otis* is not appropriate here because the retirement of the preferred was incident to liquidation.

The contention is specious, as well as inconsistent; for it seeks to confuse the *medium of payment* with the mode of determining the *amount of payment.* If the principle of *Otis* governs and, therefore, stockholders' rights are to be evaluated on the basis of a going business, it is obviously no justification for failing to do so that those rights, once evaluated, are to be satisfied in cash rather than in securities. To be sure, the fact that the preferred stockholders were not to receive new securities rendered unnecessary a determination of whether new securities were the equivalent of the rights surrendered. But the process of determining the value of those *rights,* on a going-concern basis, is no different merely because compensation is to be made in cash rather than securities.[1]

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[1] Cf. Court of Appeals' Opinion, R. 38.

That determination must be made, as in *Otis,* by evaluating the correlative claims of both classes of stockholders in the prospective earning power of the going concern. And we demonstrate *infra,* pp. 101-2, how different are the results reached if the rights of the Engineers' stockholders are actually evaluated on a going-concern basis in accordance with the principles of *Otis,* which the Commission purported to be following in this case.

Finally, it may be observed that this contention which Commission Counsel now press upon this Court is directly contrary to the Commission's own holding on this very subject in its *Georgia Power & Light Company* decision, approved and enforced by the District Court of Georgia. In that decision, the Commission squarely held that although the preferred stockholders were being paid off wholly in cash, determination of whether such cash payment represented the equitable equivalent of the preferred stockholders' rights must be made on a prospective going-concern basis in accordance with the principles of *Otis* precisely in the same manner as in the other decisions referred to above (*supra,* pp. 89-90) in which senior security holders received new securities rather than cash, and without regard to current market prices or redemption provisions.[1]

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[1] *Georgia Power & Light Co.,* Holding Company Act Release No. 5568 (1945) approved and enforced, Civil Act No. 133 (M. D., Ga., 1945), where holders of well covered $6 preferred stock of an operating utility company which was continuing in business received $150 cash upon the compulsory retirement of their preferred stock having a liquidation preference of $162.50 and entitled on redemption to $167.50 per share. The Commission stated:

> "* * * the plan before us differs from the plans which were the subjects of our earlier decisions in that it is here proposed, as already indicated, to accomplish the result required by Section 11(b)(2) by terminating all interests of the public holders of

Holdings to the same effect were subsequently made by the Commission in two other cases where senior security holders of *continuing companies* were paid out in cash.[1]

(2) If instead of relying solely on transient market values of a haphazard moment, the Commission had sought to appraise the Engineers' preferreds in terms of their average long-range record,[2] clearly no value in excess of $100 per share could be found, as both Courts below held.[3] Moreover, if it had sought to appraise their *prospective* value on a normal long-range basis and had adequately allowed for only such increase in money rates

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Georgia's preferred stock by means of a cash payment instead of continuing their interests in the enterprise by means of according them the fair equivalent of their existing rights in the form of new common stock (p. 17).

* * * * * * *

"We turn now to consider whether the cash in the proposed amount of $150 per share accords the public holders of Georgia's preferred stock the equitable equivalent of their bundle of rights *approaching the problem in a manner similar to that employed by us in testing the fairness of a plan of recapitalization with a single class of stock*" (p. 20; emphasis supplied).

[1] *National Power & Light Company*, Holding Company Act Release No. 8445 (1948), p. 16; *Pennsylvania Edison Company*, Holding Company Act Release No. 8550 (1948), p. 10.

[2] Cf. *Schwabacher v. U. S.*, 334 U. S. 182, where the Court stated (p. 200): "The Commission considered the stock's *past yield*, present market price, *and future prospects*." (Emphasis supplied.)

The failure of the Commission in the instant case to accord any attention to the past market prices and yields of the Engineers preferreds is all the more notable in the light of the fact that the Commission has repeatedly laid strong emphasis on past market history and original issue prices in the long series of cases involving retirements of senior securities for cash, where the frustration doctrine was applied (*supra*, p. 55, notes 3 and 4).

[3] District Court Findings 48-53, R. 313a-315a; Court of Appeals, R. 38: "* * * we do not believe that such a finding could be supported on the present record".

and preferred yields as have already taken place, it is equally clear that a value in excess of $100 per share could not be found. On the basis of the increase in money rates and yields alone,[1] we submit it is indisputable that the Engineers' preferreds if still outstanding would presently have an "investment value" of less than $100 per share.[2] And *all* tangible indications emphatically point

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[1] Market prices or "yields" of preferred stocks are, of course, the product of two factors: earnings and money rates. An adverse change in *either* of these factors must adversely affect the market price and yield.

Although the Commission made no attempt to consider the future earning power of the subsidiaries, the rapidity with which changes occur in the earnings of leveraged public utility common stock such as Engineers distributed to its stockholders as a liquidating dividend, is demonstrated by the decrease in earnings of Virginia. The common stockholders of Engineers received 1.45 shares of Virginia common for each share of Engineers common owned, which represented the largest item in the distribution. In 1946 (the year in which the Commission issued its opinion), earnings available for Virginia's common stock were $5,027,740, equivalent to $1.71 per share of common (Moody's, Public Utilities, 1948, p. 745). For the 12 months ended September 30, 1948, earnings available for Virginia's common had dropped to $4,062,427, equivalent to only $1.37 per share on the number of shares then outstanding, and additional shares are now being sold which will further dilute per share earnings (Moody's, Public Utilities, Current Supp.; Vol. 20, p. 1745).

[2] There are contained in the record (R. 122-123) the authoritative figures on the basis of which the Court of Appeals was requested to judicially notice the changes which have taken place in preferred stock yields, and which established that even as of that time (May, 1947) the Engineers preferreds would have had an "investment value" of less than $100 per share. Subsequent developments make this conclusion *a fortiori*, as the following data shows:

Yields on "High Grade Preferred Stock" which stood at 3.42% as of the period of Badger's testimony, at 3.75% as of the date of the District Court's Findings, at 4.12% as of the approximate date petitions for rehearing were presented to the Court of Appeals (see R. 122 for all foregoing), had risen to 4.28% as of October, 1948 (Standard & Poor's, Trade & Securities, Current Statistics Section, November, 1948, p. 27). This represents an increase of 25% in

in the direction of substantial further reductions in the foreseeable future.[1]

It is thus plain that even appraised independently of the rights of the common stockholders, $100 per share represents the *upper limit* of the preferreds' value whether viewed in the light of the record subsequent to Engineers' dissolution or in the light of the entire record prior, as well as subsequent, to dissolution.

(3) If, however, it were to be held that value predicated on current market prices is the proper basis for determining the cash amounts to which the preferred stockholders are entitled in this liquidation, then consideration must also be given to the impact of the changes which

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the yield of high grade preferreds since the time of Badger's computations.

In recognition of the fact that the Engineers preferreds were of inferior quality, Badger had estimated a yield basis of 4.6%, as compared with the much lower yields then prevailing for high grade preferreds. Applying to this 4.6% yield merely the same 25% increase which has taken place for "high grade preferreds", the present indicated yield for the Engineers preferred would be 5.75%. Since the weighted average of the dividend rate on the three series of Engineers preferreds was slightly under 5.40% (the greater portion of the preferred having been of the $5 and $5.50 series) it is evident that on the average the Engineers preferreds would now sell for less than $100 per share, even accepting *arguendo* Badger's estimate of 4.6% for the Engineers preferreds as of the time he testified. However, the Commission did not pass on Badger's 4.6% estimate (R. 67a-68a).

Moreover, the increase in the yields of low to medium grade preferreds, such as those of Engineers, would necessarily be greater than the increase on "high grade preferreds", as Judge Leahy stated (R. 314a), thus indicating a present price for the Engineers preferreds probably less than $90 per share.

Reference may be made to Public Utilities Fortnightly (December 2, 1948, p. 816), for a list of representative holding company preferred stocks selling on an average yield basis of 6.7%; some of these preferreds are the subject of recapitalization plans currently pending before the Commission.

[1] With respect to the future course of money rates, it is to be noted that the Federal Government is still actively supporting the long-term Government bond market, and that agitation in favor of aban-

have taken place in these values since the date of the valuation evidence on which the Commission predicated its finding. By the time the District Court was called upon to approve the plan, substantial changes in those values had taken place, as the District Judge found (R. 314a). He further pointed out that these changes had not been foreseen or allowed for by Badger,[1] stating:

> "These changes occurring within approximately a year of Badger's testimony do not bear out his views as to the asserted stability and 'permanence' of the low money rates, even if 'permanent' be defined as 'two to three years'. A continuance for two or three years of the trend indicated over the past year could substantially reduce or wholly eliminate the differential in the current yield rate over dividend rate in the case of preferred stocks of the type of Engineers".[2]

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donment or modification of this policy had recently been greatly on the increase. (See, for example, "Row Over U. S. 'Pegs' in Market Grows", New York Times, December 12, 1948, p. F1, col. 8; "Parkinson Assails Pegging U. S. Bonds", New York Times, Nov. 11, 1948, col. 6, p. 45; Leffingwell, "How to Control Inflation", Fortune Magazine, October, 1948, p. 90 *et seq.*, "Change Advocated in Bond-Peg Policy", New York Times, December 10, 1948, p. L41, col. 8. If any further modification should take place in the Government's present pegging policies, a further increase in money rates and preferred yields must inevitably result.

With respect to foreseeable future changes in earnings, it may be noted that if current proposals for re-imposition of some form of excess profits taxes or for a general increase in corporate tax rates should materialize, the earnings available for the common stock of the three operating companies would immediately be sharply curtailed. Prior to Engineers' dissolution these companies had the advantage of filing consolidated tax returns, which the record establishes saved the stockholders approximately $1,900,000, during the period 1941-1945 alone (R. 611a); this advantage was irretrievably wiped out in the liquidation, along with the many others (see, *infra*, pp. 117-119).

[1] Compare *Reconstruction Finance Co. v. Denver & R. G. R. Co.*, 328 U. S. 495, 521-522.

[2] R. 314a; and see the Court of Appeals' reference to the Trial Judge's cogent finding respecting Badger's money rates, R. 19.

As we have shown, the further changes in money rates which the District Judge envisaged have already taken place, although in a shorter period of time, with the result that as of the present time (as for some time in the past, R. 122-123) the "investment value" of the Engineers' preferreds is less than $100 per share. It is axiomatic that "the decree of a court of equity speaks as of the date of entry" [1] and a final decree has not been entered in this proceeding. That decree must take account of these material supervening changes, not foreseen or allowed for in the Commission's findings. *Knight v. Wertheim & Co.*, 158 F. 2d 838, 843 (C. C. A. 2, 1947), cert. den. *sub nom. McGuire v. Equitable Office Bldg. Corp.*, 331 U. S. 818 (1947). Cf. *R. F. C. v. Denver & Rio Grande W. R. Co.*, 328 U. S. 495, 521-522. It is evident that if appropriate account is taken merely of the changes which have already occurred, even on the Commission's valuation formula the preferred stockholders could not be found entitled to more than $100 per share.

C. Application of the Otis formula required an examination of the correlative rights of the preferred and common stockholders. Evaluation of these correlative rights would have resulted in payment to the Engineers preferred of less than $100 per share.

(1) Apart from its erroneous reliance upon transient market values, the Commission's determination of the equitable equivalent of the rights surrendered by Engineers' stockholders failed utterly to take account of the correlative rights of the preferred and common. Under the *Otis* formula, determination of rights on a going-concern basis requires consideration of the correlative rights of both classes of stockholders in the going con

[1] See *supra*, p. 81, n. 2.

cern; and on such basis the equitable equivalent of the rights of the Engineers' preferreds was less than $100 per share.

As has been pointed out, the Commission did not evaluate the rights of the common stockholders on the basis of a going concern or otherwise; it merely left the common to receive (upon payment of $22,000,000 additional in cash) whatever remained after paying to the preferred stockholders the amounts awarded them by "maturing" their future claim to dividends on the basis of momentary market values prevailing 1½ years prior to the liquidation, as heretofore discussed.

This process represented the antithesis of the principle enunciated in *Otis.* There the Commission and this Court refused to treat the preferreds' claim as "matured", or to measure the value of the preferred apart from the value of the common in the joint enterprise. Instead, it measured the rights of both the preferred and common in relation to one another on the basis of their proportionate rights to participate in the earnings of the continuing enterprise. As a result, although the prior claims of the preferreds to earnings were strictly maintained, the "value" of the preferred as of the time of liquidation—for which its holders were to be compensated—was carefully delimited in the light of the residual claim of the common to future earnings.

Here, the Commission wholly ignored the correlative rights of the two classes of stockholders. It simply measured the "value" for which the preferreds were to be compensated by reference to current market prices, and concluded that the common should receive whatever is left after the payment of the preferred. Consequently, the rights of the preferred were treated as though they

were "absolutes", wholly independent of and unrelated to the rights of the common. But the very essence of the "going concern" concept is that both classes of stockholders have correlative rights in that going concern. Thus, while the preferred stockholders have a right to specified dividend payments in preference to any payments to the common (a right which is itself dependent on the existence of earnings sufficient to enable the payment of dividends), the latter are entitled, upon payment of such fixed dividends to the preferred, to all the earnings of the enterprise, including the earnings resulting from the employment of the preferreds' capital in the enterprise. Consequently, evaluation of the preferreds' right to the fixed dividend payments without corresponding evaluation of the common stockholders' right to utilize the preferreds' capital which is the consideration for the dividends paid thereon, is not the evaluation of the stockholders' correlative rights "on a going concern basis" which *Otis* contemplated.

(2) It has already been shown that if the Commission had actually evaluated the Engineers' preferred stocks on a normal long range basis instead of on the basis of the peak market prices prevailing in the first few months of 1946, no value in excess of $100 per share could have been found. If, however, the Commission had evaluated the rights of both the common and the preferred stockholders in relation to one another on a going-concern basis in accordance with the formula employed by the Commission and approved by this Court in the *Otis* case, it is certain that the preferred stockholders would have received considerably *less* than $100 per share in cash value.

Here there were no arrears of dividends to delay the participation of the common stock for long years and make necessary employment of a "discount" factor such as was used in *Otis*.[1] Here the claim of the common to participate in earnings beyond the amount needed to meet the preferreds' current dividends was immediate and plenary. Assuming *arguendo* that the earnings of $10,629,724 reported by Virginia, El Paso and Gulf States for the twelve months ended June 30, 1947 (the date closest to the date of distribution of the securities and the dissolution of Engineers) are accepted as prospective "normal" earnings on a going-concern basis, the annual dividend claim of the preferreds would have entitled them to an allocation of not more than 25% of the value of the enterprise,[2] with a current cash value equivalent to approximately $70 per share of preferred stock.[3]

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[1] See *In re Securities and Exchange Comm.* (*Otis & Co.*), 142 F. 2d 411, 420-421.

[2] Total earnings available for both classes of stockholders as indicated above: $10,629,724 (Moody's Utilities, Advance Supp., Vol. 19 pp. 1904, 1921, 1910).

		Allocation	*Adjusted Allocation**
Annual dividend claim of Engineers' Preferreds (all series)	$2,119,092	20%	25%
Residual earnings for common	8,510,632	80%	75%

* There has been added to the dividend claim of the preferred 25% thereof for "loss of position" (something not considered necessary in the *United Light* decision, but approximately the percentage allowed by the Commission in *Washington Railway & Electric Co.*, Holding Company Act Release No. 7410 and *Northern States Power*, Holding Company Act Release No. 7950).

[3] As shown on the accompanying table, the approximate market value of the stocks of Virginia, Gulf States and El Paso shortly after distribution aggregated $86,768,146. Add thereto $17,000,000 of cash in Engineers treasury prior to dissolution, making total

It will be observed that such a result would have been consistent with the treatment received by senior security holders in the many plans in which the Commission has measured the rights of the security holders on a going concern basis in accordance with the principles of the *Otis* case (supra, pp. 89-90). In addition, it is to be observed that under this formula the common stockholders would have been spared the necessity of making the $22,000,000 cash contribution through the exercise of the Gulf States warrants, and would in fact have received some $12,000,000 as their pro rata share of the treasury cash accumulated through property dispositions and retained earnings of the common.[1]

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value of Engineers' assets $103,700,000. Accordingly, the preferreds' allocation of 25% would have an aggregate value of $25,925,000, or approximately $66 for each of the 392,443 shares outstanding.

	*Price Per Share 8/1/47**	*Aggregate Market Value*
Gulf States common (N. Y. Stock Exchange)	15 5/8	$29,843,250
Virginia (N. Y. Stock Exchange)	16 1/8	47,279,548
El Paso ("over-the-counter")	25 1/4	9,645,348
(All prices from Standard & Poor's Stock Guide, Sept., 1947, pp. 82, 182, 66)		
	Total	$86,768,146
As of Nov. 30, 1948, aggregate total market value as computed from Wall St. Journal of 12/1/48 was		$83,526,524

[1] It was this treasury cash ($17,000,000) plus the $22,000,000 contributed by the common stockholders through the Gulf States warrants which primarily comprised the $39,000,000 paid to the preferred stockholders.

(3) It is asserted by petitioners that since the common stockholders are the "residual" claimants, they were entitled to receive only whatever remained after paying the preferred holders "the investment value" of their stocks, "on a going concern basis", and that there was accordingly no need for the Commission to evaluate the common's rights on a similar basis—or indeed on any basis. What has been said above points the fallacy of such a contention: to speak of "residual claimants" is to speak in terms of *liquidation*, not in terms of a going concern. It is this very inconsistency which prevades and completely distorts the Commission's rationale. The preferreds' rights were viewed as though the Act did not require liquidation—indeed, as though the Act did not exist. But the common's rights were viewed merely as those of the residual claimants in the liquidation which the Act had in fact compelled, and in consequence of which, losses and deprivations had been sustained by the company and the common stockholders for many years. The liquidation of Engineers did not commence with the plan which is the subject of the instant proceedings; it merely ended there. After having been insulated from all contact with such realities throughout these years, the preferred demanded, and were awarded by the Commission in the final stages of the liquidation, compensation for their *future* high expectations, still "as though there were no liquidation and no Act". Once again the full burden of the unpleasant realities was left for the common stockholders, the "residual claimants". It was precisely to this gross inequity that the Court of Appeals pointed in stating (R. 35-6):

> "What the Commission has done is to consider the investment values of the preferreds *ex* the Public

> Utility Holding Company Act, i.e., as if the Act had never been passed. But it considered only the preferreds on this basis. It seems to have omitted consideration of the common by a similar standard. It made no finding as to the 'value' of the common stock. * * * The result is that the Commission has attempted to value the securities of Engineers both *ex* the Act and *intra* the Act."

If the preferreds' rights are to be viewed as the Commission purported to view them, *ex* the Act—i.e., without taking into account the consequences of the Act—surely neither logic nor equity will permit the common's rights to be measured on a different basis. Consequently, as the Court of Appeals pointed out, the deprivations which the common suffered in consequence of the liquidation, including the divestment of profitable subsidiaries and the long period of withheld dividends, "must be weighed into the calculation" [1] if the rights of stockholders are to be determined apart from the impact of the Act—i.e., "ex the Act". On the other hand, if the rights of the common stockholders are viewed merely as those of residual claimants in a liquidation caused by the Act, then the rights of the preferred must at the very least also be limited as in a liquidation, and without added compensation for their "disappointed expectations"; for, as this Court has stated, "enforcement of an overriding public policy should not have its consequences visited on one class with

[1] (R. 37) The Court of Appeals' statement that such losses must be "weighed into the calculation", like the term "bookkeeping", was obviously intended figuratively, in the sense that the existence of such losses should be taken into account. Petitioners' attempts to distort this statement into a command that each loss must be specifically computed and the "enterprise reconstructed" constitute a transparent device for erecting a straw man with which to grapple.

a corresponding windfall to another". *Otis & Co. v. S. E. C.*, 324 U. S. 624, 637.

It was precisely in the light of these precepts that the District Court appraised the respective rights of the preferred and common stockholders, as its opinion discloses. It pointed out that evaluation of the rights of the preferred on the basis of "investment values ex the Act", without a similar evaluation of the common was contrary to the teaching of *Otis*, stating (R. 291a):

> "The argument for payment of the premium is comparable to dealing cards off the top of a deck. When full hands (based on theoretical 'investment value') have been dealt to all the senior security holders, the common would merely get whatever happens to remain. Under the Act the interest of all investors must be considered. An emphasis on a preferred's rights must not slight the interests of a common stockholder. For if this occurs this is the direct opposite of the arguments utilized in *United Light & Power*, D. C. Del., 51 F. Supp. 217, aff'd 3 Cir., 142 F. 2d 413, aff'd *sub. nom. Otis & Co. v. Securities and Exchange Commission*, 323 U. S. 624 * * *."

On the other hand, if the claims of the preferreds are to be measured "intra the Act", i.e., in the realistic light of the fact that the Act compelled liquidation of the investment of both classes of stockholders, then, as the District Court stated:

> "There is no reason why the preferreds should get additional compensation for the termination of the lucrative dividend rate which the preferreds have received, when this termination results wholly and directly from frustration of the enterprise by governmental edict" (R. 291a).

In short, the District Court, consistently with its statutory duty to determine independently whether the plan was "fair and equitable", appraised the proposed payment of premiums to the preferred stockholders both "intra the Act" and "ex the Act", after a "careful and far-reaching examination" of all the "relevant factors" (R. 34) and "substantial equities" (R. 38) which the Court of Appeals stated must be considered. Its conclusion that the "equitable equivalent" of the rights which the preferred stockholders have surrendered cannot exceed $100 per share plus accrued dividends was, we submit, not only sound but inescapable in the light of the considerations hereinabove discussed.

V. The Commission's "investment value ex the act" doctrine as applied in the instant case is repugnant to the strict priority principle and to every concept of fairness and equity.

A. The Commission's rationale sounds the death knell of the strict priority doctrine.

Just as the Commission's decision and rationale in this case find not support but repudiation in *Otis & Co. v. S. E. C.*, as has been shown, so too petitioners' efforts to pass them off in the guise of the strict priority principle cannot withstand examination. The Commission's doctrine, as applied in this case, involves a dangerous and fundamental perversion of that principle which this Court found to be firmly embedded in the "fair and equitable" standard of Section 11(e): *Otis & Co. v. S. E. C.*, 323 U. S. 624, 634.

This is true notwithstanding that the strict priority principle was not directly at issue in this case in its narrow

technical sense as it applies to senior security holders. Engineers' plan at all times provided that the preferred stockholders would receive full payment of their entire claim in cash before the common stockholders would receive any participation: the basic issue was the *amount* of that claim and the mode of its determination if the contract provisions were to be overridden.[1]

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[1] In the light of this factor, it is evident how misplaced were the derisive statements of petitioners in the Court below that the District Court had sought to substitute "notions of colloquial equity" for the strict priority standard.

Petitioners having contended that the charter liquidation provisions should not be deemed applicable to this liquidation, the District Court gave careful consideration to "all the factors which have usually been considered in these cases" (R. 292a) in order to determine whether there existed any equitable basis to justify the award of premiums to the preferred stockholders. Starting with the assumption that under the "fair and equitable" standard (R. 287a) the preferred stockholders should not receive less favorable treatment than had been accorded senior security holders under the long line of frustration cases (referred to in the Court's Opinion, R. 287a, 292a), the Court sought to ascertain whether there existed any special equitable factors which here entitled them to receive more favorable treatment. It found that there were not, and that indeed every consideration of fairness and equity, whether in a technical or a non-technical ("colloquial") sense, interdicted the payment of the premiums (R. 292a). Thus, instead of merely resting on the long line of non-premium decisions (*supra*, p. 55, notes 3 and 4), the District Court went out of its way to be certain of observing the basic precept that "it is the function of a court of equity to do equity." *Cf.* Mr. Justice Black: "A Chapter X or § 77B reorganization court is just as much a court of equity as were its statutory and chancery antecedents." (*Vanston Bondholders' Comm. v. Green*, 329 U. S. 156, 165); Mr. Justice Murphy: "Equity looks in all directions. Only in that way can the various interests in the corporate community be adequately protected." (*Comstock v. Group of Institutional Investors*, 335 U. S. 211, 238); Mr. Justice Frankfurter: "First and last, this is a proceeding in equity, and until a decree consummating a plan of reorganization is finally signed it is the duty of a court of equity not to make itself an instrument of inequity." (*Insurance Group v. Rio Grande W. R. Co.*, 329 U. S. 602, 627). *Cf.* also *Pepper v. Litton*, 308 U. S. 295; *Taylor v. Standard Gas & Electric Co.*, 306 U. S. 307.

The bankruptcy and equity reorganization decisions which have enunciated the strict priority principle surely afford no support for the Commission's determination that the common must pay the preferred $3,200,000 in excess of the preferreds' liquidation claim specified in the corporate charter. As has been shown (supra, pp. 35-36), in such decisions the amount of the priority is invariably determined solely by reference to the contract provisions as embodied in charter or indenture. We are aware of no decisions, and appellants have referred to none, where it has been held that senior security holders in bankruptcy or equity reorganization may validly receive payments in *excess* of their contract claims.[1]

The right of junior security holders to be secure against encroachments by senior holders is an unchallengeable corollary of the strict priority doctrine,[2] dictated not only by considerations of elementary fairness but by the necessity of preserving the integrity of that doctrine even in

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[1] *Cf.* Judge L. Hand, in *Knight* v. *Wertheim & Co.*: "We cannot agree that the debenture holders had as yet any legally protected interest in the property *beyond the principal and accrued interest of their bonds* which could be weighed against the shareholders' interest. If in fact they had relied upon sharing in an equity, in the property above that amount, it was without warrant of law and constituted no reason for depriving the shareholders of whatever chance might remain of realizing upon their property." 158 F. 2d 838, 843; *cert. den. sub nom. McGuire* v. *Equitable Office Bldg. Corp.*, 331 U. S. 818. (Emphasis supplied.)

Cf. also *The United Light and Power Co.*, 10 S. E. C. 1215, 1225, where the Commission stated: "In liquidation or reorganization proceedings either in bankruptcy or in equity * * * the amount of the claim is based on its face amount plus accrued interest, without regard to any redemption premium."

[2] "Each security holder must be compensated as exactly as he can be for that which he is giving up. *But, though his cup must be filled level to the brim, it must not run over.* This much is plain." (*In re Securities and Exchange Commission* [*Otis & Co.*], 142 F. 2d 411, 419 [C. C. A. 3]. Emphasis supplied.)

its narrow sense. For, if a device be employed to permit the senior security holders to transgress the limitations of their lawful claim on one occasion, the gate will inevitably be opened for reverse transgression of those very limits on other occasions. The "strict priority principle" must then give way to some form of "the relative priority doctrine" which this Court sought in its *Los Angeles Lumber* decision[1] to excise from the law of corporate reorganization.

This danger is not something remote or conjectural, but is the inevitable concomitant of the Commission's determination in the instant case. For here, the Commission held that preferred stockholders must receive more than their contractual claim in liquidation because their dividend rate was somewhat higher than the then current going rate. Surely it follows that senior security holders must receive less than their contract preference if their dividend or interest rate at the date of liquidation is lower than the then current going rate, irrespective of the fact that more than enough assets are available to pay their contract claim in full. Since the Commission applies this same "investment value ex the Act doctrine" to bonds no less than preferred stocks,[2] this means that the holder of a $1,000 bond amply protected by assets but carrying an interest rate of 4% would be required to accept a cash payment of $800 in full satisfaction of his rights, if the Commission found that bonds of allegedly comparable quality were at that moment selling on a 5% yield basis.

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[1] *Case* v. *Los Angeles Lumber Co.*, 308 U. S. 106.

[2] As has been pointed out (*supra*, p. 64, n. 1), the first case in which the Commission applied its new doctrine involved debentures: *American Power & Light Company*, Holding Company Act Release No. 6176 (1945). Cf. Commissioner Healy's cogent development of this point at pp. 39-41 of his vigorous dissent in that case.

And in this very case, based upon the yields presently prevailing for comparable securities, as has been indicated (supra, p. 95, n. 2), the holders of the 5% and 5½% preferred stocks of Engineers should be required to return a portion of the $100 per share they have already received if the District Court's decree is not ultimately confirmed.

It is scarcely less than a mockery to assert that a doctrine which entails such results is consistent with the strict priority principle. On the other hand, if it be suggested that the charter contract rights will be revived, if need be, to assure senior security *no less* than their contractual claim, then not only does the doctrine stand condemned as "a one way street",[1] but, in addition, all petitioners' arguments here as to the inapplicability of those charter provisions in liquidations under the Act stand revealed as invalid and insincere.

B. Impact of the "present investment value" on the equity stockholders.

The full import of the Commission's doctrine can best be apprehended by considering its application to the liquidation of a holding company having "non-callable" senior securities outstanding. Such securities are not uncommon in the case of utility holding companies,[2] and necessarily

[1] *Cf.* Commissioner Healy dissenting in *American Power & Light Co.* (*supra*, p. 109, n. 2) at p. 39, n. 11.

[2] For example, non-callable senior securities of holding companies are referred to in the following decisions by the Commission: *United Light-American Light & Traction Company*, Holding Company Act Releases Nos. 6603 (1946) and 7951 (1947); *Washington Railway and Electric Company*, Holding Company Act Release No. 7410 (1947); *Public Service Corporation of New Jersey*, Holding Company Act Release No. 8002 (1948); *Philadelphia Company*, Holding Company Act Release No. 8242 (1948). See also Moody's Public Utilities, 1948, pp. a103-a104, for an extensive list of non-callable utility bonds and preferred stocks.

have a market value much higher than senior securities (such as the preferred stocks of Engineers) which are callable at stipulated prices at whatever moment such redemption is advantageous to the company and the equity security holders.[1]

It will be recalled that in the instant case Badger concluded that the "values" of the preferred, if not limited by the charter redemption provision, would have been $107, $118 and $129 per share for the respective series.[2] Therefore, if the Engineers' preferreds were non-callable senior securities, Badger's "present investment values" would have resulted in the requirement that the common stockholders pay premiums of approximately $5,000,000, instead of the $3,200,000 here ordered. And if a holding company had outstanding, as some do, bonds and several issues of non-callable preferred stocks, it is evident that virtually the entire equity of the common stockholders could be siphoned off in payment of the "present investment value" of the senior securities. In this way, little or nothing might be left for the common stock, although

[1] Petitioners' strong emphasis upon the redemption provisions of the Engineers' preferreds might serve to convey the impression that this redemption provision enhanced the value of the preferred stock. In fact, precisely the opposite is true. If there were no redemption provision, the stock would be non-callable, and the preferred holders would have been entitled to retain their relatively high dividend rate when money rates were low, without any limitation of time so long as the company continued in business. Thus, the presence of the reemption provision—allowing as it did refunding by the company of the preferred stock at a time when money rates are low—detracted from rather than added to the value of the preferred. Plainly, as the Court pointed out in *City National Bank & Trust Co.* v. *S. E. C.*, 134 F. 2d 65, 69 (C. C. A. 7): "While it is true that the payment of premium was a form of compensation to the debenture holders, nevertheless the redemption provision was for the benefit of the corporation * * *, to be exercised at its election when money rates were low.

[2] Commission Opinion R. 65a-66a.

such stock might have a very substantial value on both an asset and earning power basis which would entitle it to a large participation under every recognized liquidation or reorganization standard.[1]

It is thus evident that the "investment value" doctrine is, as the District Judge observed, comparable to "dealing cards off the top of the deck."[2] The residual claimants (the common stockholders) might well find that through no fault of their own, and in response to a statutory command to liquidate the enterprise, all the "cards" had been dealt out, leaving no hand or a very incomplete one for them if the predetermined contract limitations are violated.

It may be argued, as it was in the Courts below, that in such circumstances the Commission would avoid this

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[1] Consider, for example, a corporation with the following relatively simply capitalization:

	Par Value	*"Investment Value"*
6% Bonds (Non-callable)	$20,000,000	(3.5% basis) $34,000,000
7% Preferred Stock (Non-callable)	15,000,000	(5% basis) 21,000,000
Common Stock (Earning power $1,000,000 per annum)	10,000,000	?
Surplus	5,000,000	
	$50,000,000	$55,000,000

In the foregoing case, under a rigid application of the investment value doctrine invoked in this case, the common would be required to pay the senior security holders their "investment value" of $55,000,000, although total assets of the corporation aggregate only $50,000,000. Even if $5,000,000 were sliced off the "investment value" of the senior securities, nothing would still remain for a common stock which had a book value of $15,000,000 and an earning power of $1,000,000 per annum. And, as was pointed out, the capital structure used in this example is relatively simple as compared with that of some holding companies which have several issues of preferreds as well as bonds outstanding.

[2] *Supra*, p. 105.

result by "valuing the enterprise on an over-all basis" and "weighting" the participations of the various claimants. We must assume that the Commission would indeed see the necessity of taking measures to avoid a result so palpably inadmissible. Yet, in the Court below Commission Counsel indicated that non-callable preferred stocks would be entitled to premiums as high as 60-75 percent of their par value.[1] And in the instant case, the Commission did *not* "value the enterprise" on an over-all basis or on any other basis.[2] It merely "valued" the claim of the preferred on the basis of momentary peak market prices and accorded no consideration whatever to the value of the common on a comparable basis or otherwise. The common was simply left to receive whatever remained after the preferred were paid out in accordance with the so-called "investment value ex the Act" formula; and as the District Court correctly apprehended, under this formula little or nothing may remain for valuable common stocks in liquidations compelled by the Act.

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[1] The Commission's Reply Brief (quoted in our petition for rehearing, R. 104, n. 7) stated:

> "For example, 6% preferred stock would be worth, if non-callable, approximately \$175 on a 3.42 per cent yield basis and \$160 on a 3.75 per cent yield basis."

[2] Cf. *Consolidated Rock Products Co.* v. *Dubois*, 312 U. S. 510, 520, 524.

VI. The Commission's rationale was otherwise fallacious. The liquidation of Engineers entailed no "transfer of values" to the common, but only imposition of additional losses.

A. The Commission confused "frustration" with "appropriation".

One of the greatest fallacies in the Commission's rationale is its implicit assumption that if the preferred stockholders sustained a deprivation by reason of the compulsory retirement of their stock upon payment of $100 per share, the common stockholders necessarily became the beneficiaries of that deprivation. This embodies essentially the same stark *non-sequitur* which this Court has rejected in enunciating the principle that "Frustration and appropriation are essentially different things." [1]

In concrete terms, what the Commission and the other petitioners contend is that because the market was allegedly willing to pay a premium for preferred stocks similar to those of Engineers by reason of the fact that they carried dividend rates somewhat higher than the money rates current at the time Badger and Barnes gave their testimony, it follows that the common stockholders profited to the extent of these premiums when the preferreds were retired at $100 per share upon the company's dissolution in obedience to the Act. We submit this is tantamount to arguing that if a stock which has a $100 par or stated value on a company's books thereafter attains a market value of $110, the stock-

[1] "It is well settled in this Court that, 'Frustration and appropriation are essentially different things.' *Omnia Co.* v. *U. S.* (261 U. S. 502), p. 513" (*U. S. ex rel. T. V. A.* v. *Powelson*, 319 U. S. 266, 282).

holders' potential market gain is the company's loss; or, conversely, that if the market price of the stock drops to $90 per share, the stockholders' loss is the company's gain.

Even if it be assumed *arguendo* that when the Engineers' preferreds were retired the preferred stockholders were deprived of the theoretical opportunity of realizing a premium which the market was allegedly willing to pay for preferred stock dividend rates in excess of the then going rates, no correlative benefits accrued to the common stockholders. The low "yields" on which Badger and the Commission based their determinations had relation only to the yields of preferred stocks and other senior securities. But the Engineers' common stockholders did not receive these preferred stocks which they could offer on the market in order to realize the hypothetical "premiums"; the company was required to completely retire the preferred stocks. Nor were the common stockholders permitted to put out a new issue of preferred stock or other senior securities at the low money rates then prevailing to replace the preferred stocks, and thereby to profit by the forced retirement of the preferred.[1]

[1] It is significant that in the only two decisions subsequent to the instant case in which the Commission applied the "investment value ex the Act" doctrine in connection with the retirement of senior securities, the Commission laid strong emphasis on the fact that the companies there involved were not liquidated but were continuing in business (in one instance augmented by merger), and that in both instances the companies were permitted to replace the retired preferred stocks with other senior securities carrying a much lower money cost than the preferred stocks which were retired. Thus, in *Pennsylvania Edison Company*, Holding Company Act Release No. 8550 (Oct. 16, 1948), the Commission stated (p. 42):

> "The enterprise continues with the additional betterment of closer integration with the properties of Penelec as a consequence of the merger. And Penelec accomplished the financing

On the contrary, the common stockholders were forced to liquidate what remained of their company and to dissolve, and in that dissolution they suffered serious deprivations and losses in addition to those previously sustained.[1]

necessary to acquire Pened's assets *through the issuance of securities which in effect replaced the old preferred stock and bonds of Pened at a time when market conditions were highly satisfactory.*" (Emphasis supplied.)

And in the *United Light and Railways Company*, Holding Company Act Release No. 7951 (December 31, 1947), the Commission pointed out that the 6% non-callable preferred to be retired would be replaced by an issue of ten year serial notes carrying an interest charge of only 3⅛%, and stated (p. 37):

"It may be noted that the common stockholders of American would realize substantial benefits from the elimination of the preferred at a price of $33 per share. To the extent that preferred shares are tendered, there will be a substantial reduction in charges, representing the difference between the present dividend of 6% and 3⅛% interest on the proposed serial notes. The use of debt instead of preferred stock, will also give the company certain tax advantages * * *. Since the payment to the preferred amounts to $8 per share over par * * * the entire excess over par would be equalled through savings in charges in just over five years."

Since the Commission found that these factors were highly significant in appraising the fairness of the premium payments in the plans referred to above, it would seem that petitioners are estopped from even suggesting that their complete absence here is not equally significant respecting the unfairness of the Commission's requirement for payment of the premiums in the instant case.

[1] Thus, in addition to the financial losses suffered in carrying out the Commission's divestment orders (*supra*, pp. 60-61) the common stockholders sustained the further deprivations attendant upon entirely giving up the holding company form of organization, the financial advantage of filing consolidated tax returns (*supra*, p. 96, n. 1), the centralized expert service organization, the leveraged capital structure and the recoupment of past losses which such structure would produce in an economic upswing. Some of these factors have been summarized as follows:

"As Engineers was constituted prior to the passage of the Act it had * * * the advantages of diversity (which Dr. Badger, the only witness for the preferred stockholders, admits are of value [Dr. Badger, Tr. p. 1495]), the advantages of a non-profit

Indeed, the compulsory retirement of the preferred itself constituted a serious deprivation to the common. Under their contract with the preferred, the common stockholders had the absolute right to the use of the $39,000,000 of capital contributed by the preferred without limitation of time; and without obligation other than to pay the preferred the stipulated dividends when earned. The fact that the dividend rates payable to the preferred might have been somewhat higher than those temporarily current in the money markets in 1945 and 1946 did not make this contract disadvantageous to the common. The same contract gave the common the option to retire the preferred upon payment of the redemption prices whenever the condition of the money market made such a step desirable for the common.

But even apart from this right, it would have been highly advantageous to the common to have been permitted to keep Engineers in existence and to maintain the preferred stock outstanding. The dividend rates being paid to the preferred represented an annual senior money cost, or rental charge, of 5.40% which the common stockholders paid for the use of this $39,000,000 of capital. At the time of the retirement of the preferred, as well as at the present time, many sound util-

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mutual service organization furnishing services of trained experts (Dr. Badger admits that the Engineers companies have had excellent management [Dr. Badger, Tr. p. 1699]), savings from combined purchasing, sales development and other services, leverage from the inclusion of $40,000,000 of preferred stock in the capital structure (as a preferred stock having no maturity date), a pool of credit available to aid companies whose earnings are temporarily depressed and to help equalize the earnings of the system. As a result of the Act all these advantages have been or must be foregone" (Extract from brief dated August 19, 1946, filed by Engineers with the Commission).

ity operating common stocks were available for purchase at a price equal to approximately eight times current earnings,[1] or equivalent to approximately 12½% on cost. Thus, if not for the Act, Engineers' common stockholders would have been free to retain the capital of the preferred holders without any limitations of time at an overall cost of approximately 5.40% while realizing some 12½% on this capital; or, in the alternative, the common stockholders had the option of calling the preferred stock and replacing it with preferred carrying an even lower dividend rate.[2]

Not only were the common deprived of this perpetual opportunity to retain this large reservoir of capital and to employ it profitably, but, over a period of ten years, they were forced to sell off a large number of the company's assets at a loss in order to comply with the Commission divestment orders,[3] and to retain the proceeds

[1] From the figures set forth in note 3, p. 101, *supra*, it will be seen that the common stocks of the three operating companies distributed in the Engineers liquidation were themselves accorded a market price equivalent to approximately eight times their then current annual earnings (annual earnings $10,629,724, aggregate market price $86,700,000; their present market price is approximately $3,000,000 less [*Ibid.*]). See also Public Utilities Fortnightly, issue of December 2, 1948, at p. 815, for list including many representative utility common stocks purchaseable at eight times earnings and even less.

[2] Cf. District Court Finding No. 46 (R. 311a-312a).

[3] See District Court Opinion, R. 290a; Findings 37-38, R. 307a-308a; Court of Appeals Opinion, R. 36, 37.

Apart from the losses sustained on divestments, the Act put an end to the further growth of the Engineers system which would undoubtedly have resulted in additional large earnings for the common. The record establishes that Engineers was in an excellent position to resume the process of further expansion which the depression had interrupted. One instance of this growth possibility was the option it held giving it the right to acquire control of El Paso Natural Gas Company, an enterprise which was relatively in its infancy in 1930

of those sales and forego all dividend income [1] in order to attempt to accumulate the money required to retire the preferred stock. Since the sums thus realized were still not sufficient for the purpose, the common stockholders were subsequently required to contribute $22,000,000 additional in cash, and to "mortgage" the remaining assets by advance payment of dividends [2] in order to complete the formidable task of raising the money required to retire the preferreds.

Finally, as compensation for all these efforts and deprivations, the common stockholders ultimately realized in the liquidation an amount barely approximating the sum actually received by the company for the common stock,[3] as compared with the approximately $190 paid to the preferred stockholders for each $96 received by the company.[4]

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when the option was acquired (R. 508a-510a). This company has since become one of the leading natural gas pipe line companies of the country, with total assets exceeding $102,000,000 (Moody's Public Utilities, 1948, p. 661), as compared with $7,000,000 in 1930 (Moody's, 1931, p. 2362); and net income of $283,000 in 1930 had increased to $3,953,000 in 1947 (*ibid.*). Engineers was prohibited by the statute from adding this highly promising enterprise to its system, and was ordered by the Commission to divest itself of all relationship therewith (*Engineers Public Service Co.*, 12 S. E. C. 41). Although Engineers recorded a book profit on this divestment, the record establishes that it was deprived of the opportunity to realize approximately $4,000,000 (which amount has now increased to approximately $7,000,000) additional as measured simply by the market price which the stock subsequently attained (R. 509a). More important, it was forced to forego all the advantages accruing from complete control of one of the country's most dynamic growth situations.

See also Findings 37-38 (R. 307a-308a), and Court of Appeals Opinion (R. 36-37).

[1] Commission Opinion (R. 69a); District Court Findings 34-36, R. 306a-307a.

[2] Cf. District Court Findings 39-40 (R. 308a-309a).

[3] Cf. Engineers Ex. No. 54, R. 1820a, and District Court Finding No. 31, R. 305a.

[4] District Court Findings 23-26, R. 301a-303a.

B. Petitioners' contention that the common stockholders derived "economic benefit" from the retirement of the preferred is frivolous.

In the face of these facts it is understandable and significant that petitioners find it necessary to attempt an argument that the retirement of the preferred stocks resulted in countervailing "economic benefit" to the common.[1] The only basis which can be suggested for this contention is a sentence in the Commission's opinion to the effect that "the retirement of the preferred stock will be of immediate benefit to the common stockholders" (R. 69a), a sentence which merely serves to highlight the inconsistencies and paradoxes flowing from the Commission's fictional doctrine. For, examination of the context in which this statement appears, makes it incontrovertibly plain that the Commission merely recognized that the impact of Section 11 on Engineers had been so severe, and the degree of governmental frustration of the enterprise so great, that the preferred stock had been transformed *as the result of the Act* into a burden for the common stockholders, instead of the valuable advantage it had formerly constituted and would at present constitute if not for the Act.[2]

It is indisputable that the preferred stock became a "financial burden" only because the Act itself prevented the company from realizing income on the $39,000,000

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[1] Petition of the Commission in No. 266, pp. 6, 17.

[2] The Commission's own words foreclose argument on this point. It stated (R. 59a):

> "The reduction of the Engineers holding company system from its previous size and diversity to a single operating company necessitates a commensurate contraction of its financial structure. Engineers' outstanding preferred instead of providing valuable leverage for the common, has become a financial burden."

of capital which that stock represented. Even in the face of the sacrifices imposed on Engineers during the decade following passage of the Act, it would still have been greatly to the advantage of the common stockholders, as we have shown (supra, pp. 117-118), if they had been permitted, free of the Act's restraints,[1] to retain their enterprise alive, to continue the preferred stock outstanding, and to invest the $39,000,000 in the stocks of operating utilities. But again the Act intervened to impose upon them the further and final requirement—the complete dissolution of the remainder of the enterprise. Under these circumstances, to refer to the "benefits" conferred by the Act upon the common by reason of the retirement of the preferred stock which the Act alone had transformed from a valuable asset (as the Commission itself stated) into a burden, *at best* partakes of that bizarre "exercise in semantics" to which Judge Leahy referred in stating (R. 311a-312a):

> "Analysis of the value of the Engineers preferreds on a 'going concern' basis is largely an exercise in semantics, since the Act dictates the dissolution of Engineers and of the entire holding company enterprise, and thus makes impossible the 'going concern'

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[1] The inability of Engineers to reinvest the proceeds realized from the sale of assets pursuant to the Commission's divestment orders was due solely to the restrictions contained in the Act. Under Sections 9 and 10, no new acquisitions may be made by a holding company except with the approval of the Commission, which may be granted only in very special circumstances. And the record establishes (R. 448a, 978a) that apart from one relatively modest acquisition in connection with Virginia, Engineers was unable to make any others within the statutory limitations. Cf. *The Western Public Service Company*, 12 S. E. C. 804, concurring opinion, at p. 818: "The management apparently has found no lawful way in which this capital can be reinvested in furtherance of the purposes for which this corporation was created. The fair course is to return it."

in which the preferred and common stockholders engaged to invest. If not for the requirements of the Act, Engineers as a 'going concern' would have been free to take advantage of the present low money markets by calling and redeeming its preferred stocks and replacing them with preferred stocks carrying a lower dividend rate than those now outstanding; it would thus continue to enjoy the leverage advantages of senior capital, but at a substantially lower cost. Under these circumstances, payment of the premiums to the preferred stockholders would have been consonant with the purposes and intent of the charter redemption provision. But the Act has made it impossible for the Company and the common stockholders to avail themselves of these benefits contemplated by the contract, along with the many other advantages which would have accrued to them as a 'going concern, exclusive of the impact of Section 11'."

As has previously been shown (supra, pp. 54-59), prior to the adoption of its "investment value ex the Act" doctrine applied in this case, the Commission had itself recognized and forcefully urged in the courts that "fairness and equity" require consideration of the correlative deprivations which the junior security holders sustain along with the senior security holders in consequence of the retirement of the latter's investments under the impact of Section 11, and that such consideration renders unfair and inequitable the payment of premiums. The Commission's pertinent statement in its brief in *New York Trust Co.* v. *S. E. C.*[1] merits repetition here:

"In the instant case neither Power nor a successor company is retaining, or can retain, the capital ob-

[1] 131 F. 2d 274 (C. C. A. 2), cert. den. 318 U. S. 786, rehearing den. 319 U. S. 781.

> tained from the sale of the debentures for the benefit of the system. The debenture holders are being repaid the principal of and accrued interest on their debentures, are restored to their original position, and are not compelled to accept the risks of a new enterprise. Under these circumstances as we have heretofore shown the debenture holders are not entitled to anything more."

Although the foregoing argument was presented to the Second Circuit some years before the Commission's decision in the instant case, the Commission has again recognized the soundness of the basic reasoning therein contained in its two recent decisions referred to supra, p. 115, n. 1, in which it emphasized that payment of the premium was "fair and equitable" to the junior security holders because, *unlike the situation here,* the common stockholders in those cases were permitted to continue their enterprises in existence and to replace the retired senior securities with other senior securities at a much lower rate.

PART THREE

THE DISTRICT COURT DID NOT EXCEED ITS STATUTORY FUNCTIONS. THERE WAS NO VALID BASIS FOR REMANDING THE PROCEEDINGS TO THE COMMISSION.

VII. The District Court did not exceed its powers in subjecting to an independent examination the Commission's conclusion that the plan was fair and equitable.

The Commission contends, as it did in the court below, that unless its conclusion upon the fairness and equity of a plan under Section 11(e) lacks "any rational and statutory foundation", it may not be disturbed by the District Court, and that the Commission's judgment in these matters may not be reversed by the District Court unless "it has plainly abused its discretion". The Court below rejected that contention, and after the most careful analysis of the Act, its legislative history, the relevant authorities and other considerations (R. 20-34), concluded:

> "In the light of the foregoing we cannot hold, as the Commission contends that we must, that unless the conclusions of the Commission lack rational or statutory foundation they may not be disturbed by the Section 11(e) court, or that a reversal of the Commission's judgment by the court may not be effected save where the Commission has plainly abused its discretion. We conclude that it was the duty of the court below to function as an equity reorganization tribunal within the limitations prescribed by the Act. The findings and conclusions of the Commission were not binding upon the learned District Judge though, as was proper, he treated them with respect" (R. 34).

It is our position that even under the most restrictive view of the jurisdiction of the District Court in these matters, its judgment in the present case was correct and should be affirmed, since the conclusion of the Commission that the plan was fair and equitable was without rational and statutory foundation. To reach its determination that the plan as approved by the Commission was not fair and equitable, the District Court was not required to disturb, and did not disturb, any factual finding of the Commission. Virtually all the facts upon which the District Court rested its conclusion had been found by the Commission. No attack was made in the courts below, and so far as we are aware none is made here, by any party, upon the accuracy of the facts recited in the District Court's opinion or in its findings.[1] The District Court differed with the Commission's ultimate conclusion, based upon the admitted and undisputed facts as set forth in the Court's opinion and findings. And, where the *conclusion* of the Commission upon the facts is, as here, either without rational basis or contrary to law, even a "review" court exercising the most limited review functions would have the power to set aside the conclusion.

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[1] The record establishes that at the hearing before the District Court held May 29, 1947 (R. 384a-349a) the Court invited the parties to suggest any amendments they might wish to the findings, either orally or pursuant to the procedure provided by Rule 52(b) of the Rules of Civil Procedure. Except for several very minor items suggested by Commission Counsel and accepted by the Court (R. 389a), no requests for amendment or contentions as to inaccuracy were made either at that hearing or at any time thereafter. Cf. Rule 52(b), Rules of Civil Procedure.

The Court of Appeals having affirmed the "careful and far-reaching examination of the relevant factors" made by the District Court (R. 34), these findings are "final here in the absence of a very exceptional showing of error". *Comstock* v. *Group of Investors*, 335 U. S. 211, 214.

However, we do not concede that the power of the District Court under Section 11(e) is as limited as the Commission contends it should be. On the contrary, we submit that the District Court and the Court of Appeals were clearly correct in holding that the District Court is required under Section 11(e) to exercise an independent judgment as a court of equity in determining whether a proposed plan is fair and equitable. We think this is clearly demonstrable from the language of the statute itself, from the judicial and legislative history of the words employed in the statute, from the construction which the Commission itself has heretofore placed upon the statute, and from the judicial construction the statute has heretofore received.

A. Internal evidence from the Act itself.

Section 11(e), in outlining the respective functions of the Commission and of the District Court, with respect to a plan submitted by the company, uses substantially identical language in the two instances. As to the Commission the language is:

> "If, after notice and opportunity for hearing, the Commission shall find such plan, as submitted or as modified, necessary to effectuate the provisions of subsection (b) and fair and equitable to the persons affected by such plan, the Commission shall make an order approving such plan; * * *."

As to the District Court the language is that if, upon application by the Commission at the request of the company to enforce and carry out the terms and provisions of such plan,

> "* * * the court, after notice and opportunity for hearing, shall approve such plan as fair and equi-

> table and as appropriate to effectuate the provisions of section 11, the court as a court of equity may, to such extent as it deems necessary for the purpose of carrying out the terms and provisions of such plan, take exclusive jurisdiction and possession of the company or companies and the assets thereof, wherever located; * * *."

As the Court of Appeals said: "The words employed respecting the respective duties of Commission and court are so alike that we must conclude that Congress intended to lay substantially the same duty on the court in the second instance as it imposed on the Commission in the first" (R. 24). "One may not presume that the same words employed in a single subsection of a statute have dissonant meanings" (R. 25).[1]

It will be observed that, in addition to the findings that the plan is fair and equitable, which both the Commission and the District Court are required to make, the Commission must also find that the plan is "necessary" to effectuate the provisions of subsection (b), and the District Court must find that the plan is "appropriate" to effectuate such provisions. This difference, in defining the respective duties of Commission and Court in relation to the *public* issues involved in the determination of whether the plan conforms to and furthers the aims of the Act, emphasizes the co-ordinate jurisdiction accorded to Commission and Court in relation to *private* interests affected by the plan, namely, whether the plan is fair and equitable to the respective security holders.[2]

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[1] See *Davies Warehouse Co.* v. *Bowles*, 321 U. S. 144, 150.

[2] Compare the same distinction with respect to the powers of the Interstate Commerce Commission and the district courts under Section 77 of the Bankruptcy Act, discussed, *infra*, at pp. 130-133.

Other provisions of the Act confirm the conclusion dictated by the central provisions above quoted, and serve to differentiate the character of the jurisdiction accorded to the District Court under Section 11(e) from that accorded to the Court of Appeals under Section 24(a), the section which petitioners seek to merge into 11(e). Section 24(a) prescribes that "the findings of the Commission as to facts, if supported by substantial evidence, shall be conclusive." This limitation is pointedly omitted from Section 11(e). Section 11(e), on the other hand, expressly directs that the proceedings in the District Court shall be "after notice and opportunity for hearing", which has been construed to require that notice be given to all security holders who may be affected, many, if not most of whom, will not have appeared before the Commission (R. 26).[1] There is no such requirement with respect to proceedings under Section 24(a); on the contrary, that section provides that no objection to the order of the Commission shall be considered by the Court unless such objection shall have been urged before the Commission or unless there were reasonable grounds for failure so to do.

We believe it was in recognition of this clear statutory scheme as to the plenary co-ordinate rôle of the District Court under Section 11(e) that this Court stated:

> "Any plan of divestment or reorganization, moreover, must be carefully scrutinized by both the Commission and the enforcing court, thus enabling the assertion and protection of all shareholders' rights." North American Co. v. S. E. C., 327 U. S. 686, 709.

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[1] *In re SEC (Otis & Co.)*, 142 F. 2d 411, 422 (C. C. A. 3, 1944).

B. The function of the District Court in equity reorganizations and bankruptcies.

Passing from the Act itself to consider extrinsic evidence on the meaning of the terms employed, we find that the words "fair and equitable" were "words of art" which had long before "acquired a fixed meaning through judicial interpretations in the field of equity receivership and reorganizations".[1] Shortly prior to the passage of the Act this Court had declared, "Every important determination by the Court in receivership proceedings calls for an informed, independent judgment".[2]

The phrase "fair and equitable" with its "fixed meaning" so well established was carried over into bankruptcy reorganizations under Section 77B [3] and into railroad bankruptcies under Section 77.[4] It has the same meaning as used in the Holding Company Act.[5]

While it must be obvious from a comparison of Section 11(e) of the Holding Company Act with Section 77 of the Bankruptcy Act that the power of the District Court under the former is broader than under the latter statute, it is established that even under the latter statute the District Court is not merely a "review court" which is required to approve a plan of reorganization as fair and equitable unless it finds the determination of the Interstate Commerce Commission to that effect to be lacking in "any rational and statutory foundation".

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[1] *Case v. Los Angeles Lumber Co.*, 308 U. S. 106, 115 (1939).

[2] *National Surety Co. v. Coriell*, 289 U. S. 426, 436 (1933); *First Nat. Bank v. Flershem*, 290 U. S. 504, 525 (1934).

[3] *Case v. Los Angeles Lumber Co., supra.*

[4] *Ecker v. Western Pacific R. Corp.*, 318 U. S. 448, 482 (1943); *Group of Investors v. Milwaukee R. Co.*, 318 U. S. 523, 542 (1943).

[5] *Otis & Co. v. S. E. C.*, 323 U. S. 624, 634 (1945).

Certain functions are, by Section 77, lodged exclusively in the Interstate Commerce Commission and withdrawn from the jurisdiction of the District Court. Valuation of the debtor's property is one such area where the Interstate Commerce Commission is supreme; the function of the District Court is limited to determining whether the Commission observed statutory mandates.[1] Other matters, such as abandonment of property or forfeiture of leases, where the public interest is dominant, are similarly treated.[2] But these decisions rest upon express language contained in Section 77 of the Bankruptcy Act which has no counterpart in Section 11(e) of the Holding Company Act. This Court has recognized that "the whole scheme of Section 77 leaves no doubt that Congress did not mean to grant to the district courts the same scope as to bankrupt roads that they may have in dealing with other bankrupt estates".[3]

However, in the field where the district courts were granted participation with the Interstate Commerce Commission, the district courts are expected to act *independently* and not as courts of review over the action of the Commission. This is particularly true with respect to claims of priorities among security holders where the interests at stake are mainly private rather than public. In *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448 (1943), where the respective functions of the Interstate Commerce Commission and the District Court were fully considered, this Court said (p. 479):

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[1] *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448, 472 (1943).

[2] *Palmer* v. *Mass.*, 308 U. S. 79 (1939); *Smith* v. *Hoboken R. Co.*, 328 U. S. 123 (1946).

[3] *Palmer* v. *Mass.*, 308 U. S. 79, 87 (1939).

"For example, there may arise controversies over the priority or the validity of claims. A Commission finding involving such problems would require an independent examination and an affirmation by the court."

What this Court meant by an "independent examination" is made clear by its discussion on the question of valuation; after pointing out that the statute vests in the Interstate Commerce Commission the function of valuation "without participation by the [district] court", this Court nevertheless stated that "this valuation must be made in accordance with the direction of the statute and as to that valuation is subject to judicial review", which review is "limited in character" and "does not involve an independent examination into valuation" (p. 477).[1]

In *Group of Investors* v. *Milwaukee R. Co.*, 318 U. S. 523 (1943), decided with the *Ecker* case, this Court did not again discuss the respective functions of the Interstate Commerce Commission and the District Court, but the opinion is replete with references to the important functions to be exercised by the District Court in railroad bankruptcies. Repeatedly the Court adverts to and relies upon the fact that the District Court had affirmed certain relevant findings of the Commission.[2] Speaking of the difficulties inherent in bringing two divisional

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[1] A similar distinction, made by the District Court in the *Ecker* case, between the review powers exercised by the District Court upon the Commission's valuations on the one hand, and the "independent judgment" exercised by the District Court upon other findings of the Commission on the other hand, was approved by this Court (p. 467).

[2] Pages 537-538, 541, 546-556 *passim*.

mortgages into a new capital structure, this Court observed that, "The question in each case is one for the informed discretion of the Commission *and the District Court*" (p. 564; emphasis supplied), and it differentiated sharply between the functions of the District Court in that respect and the "review functions" of this Court:

> "The District Court satisfied itself that the principles of priority as applied to these facts were respected. See 36 F. Supp. pp. 202-203, 211-212. Since such a determination rests in the realm of judgment rather than mathematics, there is an area for disagreement. But we are not performing the functions of the District Court under § 77(e). Our role on review is a limited one. It is not enough to reverse the District Court that we might have appraised the facts somewhat differently. If there is warrant for the action of the District Court, our task on review is at an end" (p. 564).

Again, speaking on the question whether the plan was "fair and equitable", this Court said:

> "Whether in a given case senior creditors have been made whole or received 'full compensatory treatment' rests in the informed judgment of the Commission and the District Court on consideration of all relevant facts" (p. 566) [1]

In *Comstock* v. *Group of Institutional Investors*, 335 U. S. 211, this Court again recognized the "broad responsibility laid upon the [District] Court for the equity

[1] See also the similar statement that: "The earnings periods to be selected and the methods to be employed in allocating earnings among the various divisions are matters for the informed judgment of the Commission and the District Court" (p. 572).

and fairness of the plan as a whole" in proceedings under Section 77 of the Bankruptcy Act and declared:

> "The court will be diligent to protect itself and the public from approval of unfair plans, even by default, and may take for its own use evidence no party would have a right to force upon it" (pp. 227-228).

The legislative history of Section 77 had previously been traced in *Palmer v. Massachusetts,* 308 U. S. 79 (1939). The Court recalled that, "There was a strong sentiment in Congress to withdraw from the courts control over insolvent railroads and lodge it with the Interstate Commerce Commission. Congress stopped short of this remedy" (p. 87).[1]

Bearing in mind that Congress in 1933 refused to lodge with the Interstate Commerce Commission exclusive control over insolvent railroads notwithstanding the more than 40 years of experience which that administrative body had had with every detail of railroad finance and management, it would be surprising indeed if Congress should have intended in 1935, when it enacted the Holding Company Act, to vest greater control over the rights of stockholders in reorganization and liquidations of utility holding companies in the Securities and Exchange Commission, then a newly organized agency with no experience whatever in the regulation of utility holding companies or in corporate reorganizations generally.

C. Legislative history of the Act.

The legislative history of the Holding Company Act bears out the foregoing conclusions. The Senate Committee which reported out the original bill stated:

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[1] See also *Ecker v. Western Pacific R. Corp.,* 318 U. S. 448, 468-470 (1943).

"Section 11 provides that plans for the voluntary readjustment of the affairs of holding companies to conform with the section may be presented to the federal courts at any time and that in such cases those courts may exercise in the furtherance of such voluntary plans *all the extraordinary powers such courts have been accustomed to exercise when called upon under the Sherman and Hepburn Acts to effect compulsory corporate readjustments required by the public policy expressed in those acts* * * *. The title provides that *during all court processes the Securities and Exchange Commission shall act as an impartial expert economic adviser and administrative assistant to the courts.* That expert assistance will enable the courts to save time and expense in the solution of essentially economic and administrative problems for which in the Sherman Act cases it had no assistance except that of opposing counsel."[1] (Emphasis supplied.)

Clearly the "extraordinary powers" exercised by the District Courts under the Sherman and Hepburn Acts were the plenary powers of a court of equity; and it was contemplated that the Commission, "as the impartial, expert, economic adviser and administrative assistant to the courts" would not diminish or encroach upon the functions to be exercised by the courts.

The sharp debate which occurred in the Senate around the provision contained in the bill (S. 2796) that would have required the District Court in proceedings under subdivisions (d), (e) and (f) of Section 11 to appoint the Commission as trustee, and which resulted in amending the bill so as to make the duty to appoint the Commission as trustee permissive and not mandatory, brought into sharp focus the Congressional intention that the

[1] Senate Report No. 621, accompanying S. 2796, 74th Cong., First Session, pages 13 and 14; emphasis supplied.

jurisdiction of the District Courts in proceedings under those subdivisions should be the traditional jurisdiction of a court of equity in reorganization proceedings.

Senator Wheeler, who had charge of the bill in the Senate, sought to assure that body that

> "* * * the provision does not oust the jurisdiction of the court at all, because the court has to approve the plan even though the Commission approves it. In other words, there is really a double check upon the plan, and final determination rests as in the past in the courts."[1]

Nevertheless a number of Senators continued to hammer the point:

> "Senator Clark: 'I say that I very violently disagree with the theory * * * that any sort of a Commission functioning from Washington through emissaries or agents, or attorneys, is to be preferred in its discretion to a federal judge appointed to one of the very highest honors in this country, appointed by the President, usually after careful and most meticulous selection and confirmed by the United States Senate * * *.[2] The Commission ought to be made a party, given the right to be heard, given a standing in court, but it should not be mandatory on the court to accept the Commission's ukase.'[3]
>
> * * * * * *
>
> Senator McKellar: 'I believe in courts. Sometimes they do wrong of course; they sometimes fail to do what they ought to do. They are not perfect; but neither are Commissions perfect. From my experience with Commissions and with courts, I believe I would rather trust the courts.'"[4]

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[1] 79th Cong. Rec. 8845, 74th Cong., First Session.

[2] p. 8939, Cong. Rec., *supra*.

[3] p. 8940, Cong. Rec., *supra*.

[4] p. 8939, Cong. Rec., *supra*.

Senator Barkley, replying to a previous statement by Senator McKellar, had stated:

> "I appreciate the force of what the Senator says. Of course, this is an administrative duty of the court. It is not like *telling the court how to decide the law, or as to equities among investors or how a reorganization shall be brought about.* The appointment of receivers is an administrative matter which is performed by the courts." [1]

And in the end, notwithstanding the repeated assurances by the proponents of the measure that there was no intention to impinge upon the traditional independence of the district courts as courts of equity in the reorganization proceedings contemplated by subsections (d), (e) and (f) of Section 11, Senator Wheeler found it necessary to agree to the amendment, which was embodied in the statute as finally enacted.[2]

D. The Commission's interpretations of the Act prior to this case.

The Commission itself, prior to this case, has not contended that the District Court in a Section 11(e) proceeding is merely a "review court" which must approve the Commission's determination "unless wholly lacking in a rational or statutory basis". On the contrary, it has constantly stressed the *co-ordinate* role of the District Court. The following examples illustrate the position of the Commission prior to the present case.

In its 10th Annual Report to Congress (dated April 21, 1945) the Commission stated, at pages 65, 66:

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[1] p. 8937, Cong. Rec., *supra;* emphasis supplied.

[2] See p. 8939, Cong. Rec., *supra.*

> "Thus, security holders have the protection of findings as to the fairness and equity of plans by both the Commission and a United States District Court. * * *
>
> * * * * * *
>
> As has been said, security holders are not required to accept Section 11(e) plans unless they are found fair and equitable by both the Commission and a United States District Court."

At hearings by a committee of the House of Representatives to consider whether the Act required amendment, Mr. Ganson Purcell, then Chairman of the Commission, and Mr. Milton H. Cohen, then Director of its Public Utilities Division, testified as follows:[1]

> "Mr. Purcell: As I said, his new interest (the stockholder's) is gaged by his claim under the old security and his treatment must be found by the courts and the Commission to be fair and equitable.
>
> Rep. Henshaw: You say by the courts?
>
> Mr. Purcell: Oh, yes. In a Section 11 proceeding, which is the one most often resorted to by the companies, their plan is filed, and they ask, in almost all instances, that under the provisions of Section 11(e), the Commission seek enforcement of the plan in a district court of the United States. The district court is then required to find under Section 11(e) that the plan is fair and equitable, and proper to carry out the provisions of Section 11(e). That decision of the district court is in turn appealable, and it can be taken to the Court of Appeals and to the Supreme Court of the United States" (p. 873).

[1] Hearings before the Securities Subcommittee of the Committee on Interstate and Foreign Commerce, House of Representatives, on "Operations Pursuant to the Public Utility Holding Company Act of 1935", Part 3 (79th Cong., 2d Sess., 1946).

> "Mr. Cohen: The machinery of Section 11(e) of the Act provides that when the Commission finds a plan fair and equitable, it may at the request of the company, apply to an appropriate Federal district court for enforcement of the plan.
>
> Such Federal district court, on the basis of the record made before the Commission, holds full hearings on the plan, including briefs and oral argument, and then such court has the *independent duty* of determining whether the plan is fair and equitable and appropriate to effectuate the provisions of Section 11(b)" (p. 962; emphasis supplied).

Judge Leahy, who had passed on almost half of the 63 Section 11(e) plans presented to the District Courts for enforcement and had thus had the benefit of Commision counsel's presentations frequently over the past six years, stated in his opinion in *Re Interstate Power Co.*, 71 F. Supp. 164, 161 (1947):

> "Since one of the earliest cases for Federal district court enforcement under the Act was brought to me for consideration and approval, it has been consistently conceded by all parties, including the various sets of attorneys for the SEC, in this and in all other cases brought to the enforcement court, that a § 11(e) court has the affirmative and independent duty to consider and find whether a proposed plan is fair and equitable * * *."

In opening the argument of the present case in the District Court, Commission counsel conceded that: "* * * it is the independent duty of the Court apart from any objections which may have been filed, to satisfy itself that the plan meets the statutory tests of necessity as well as fairness, * * *" (R. 191a).

In its memorandum submitted to the Court of Appeals in *Lownsbury* v. *S. E. C.*, 151 F. 2d 217 (C. C. A. 3, 1945), the Commission analogized the relationship between itself and the District Courts with respect to subsections (d), (e) and (f) of Section 11, to the relationship between the Interstate Commerce Commission and the courts under Section 77 of the Bankruptcy Act, and the Commission carefully distinguished between the functions of the District Court with respect to orders made under the three enumerated subsections and the functions of the Court of Appeals in reviewing other orders pursuant to Section 24(a):

> "Congress contemplated that reorganization techniques should be available for compliance with Section 11(b) orders, and subsections (d) and (e) are in many respects a self-contained reorganization statute with provisions defining the respective reorganization functions of court and agency which are comparable to the relationship between the Interstate Commerce Commission and the courts prescribed in the previously enacted Section 77 of the Bankruptcy Act. Section 11(f) provides for a similar allocation of function as between the Commission and a reorganization court where the court's reorganization jurisdiction stems from sources other than the Holding Company Act" (p. 16).

> "An order of the Commission approving the plan, which is to be operative only if subsequently approved by a district court pursuant to subsections (d) and (e) or under some independent source of jurisdiction recognized in subsection (f), stands on an entirely different footing from the ordinary order of the Commission for which the review provisions of Section 24(a) were evidently intended * * *" (p. 17).

Virtually identical statements were made by the Commission to this Court in its brief in opposition to certiorari in the *Lownsbury* case.[1]

In the face of the foregoing, the Commission finds itself constrained to avow:

> "The Commission agrees with much of what the Court below states concerning the intention of Congress to have the Section 11(e) court function as an independent check upon the Commission's determination that a plan is fair and equitable and also that the respective roles of the Commission and enforcement court should be in general similar to the relationship under Section 77 of the Bankruptcy Act between the Interstate Commerce Commission and the reorganization court."[2]

Having thus made obeisance to its own recorded statements, the Commission thereupon nevertheless proceeds to contend that the "independent role" of the District Court under Section 11(e) is no broader than that of a review court under Section 24(a), and that the District Court is bound by the Commission's conclusions unless they wholly "lack a rational and statutory foundation".

This is to give a new and surprising meaning to the term "independent", and one which scarcely seems supported by the careful distinction drawn by this Court between the functions of a review court and the independent role of the District Court in passing on the fairness and equity of plans under Section 77 of the Bankruptcy Act (*supra*, pp. 131-2).

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[1] *Lownsbury v. S. E. C.*, No. 1245, October Term, 1944, Brief of the Securities and Exchange Commission, pp. 7, 9.

[2] Commission petition, No. 226, p. 22.

E. Other authorities.

Although the precise question here under discussion has not been authoritatively determined, probably because the Commission has never, before this case, contended for the interpretation which it now asserts, there have been expressions in the lower courts recognizing that the District Courts, in passing upon Section 11(e) plans, exercise an independent and plenary equity jurisdiction.

In *Commonwealth and Southern Corp.* v. *S. E. C.*, 134 F. 2d 747, the Court of Appeals for the Third Circuit "took the position that stockholders, whose rights were affected by an order of the Commission directing a public utility holding company to change its corporate structure had a right to a full hearing in the District Court of the United States in which the Commission was seeking approval of the reorganization plan" (R. 32). In *In re SEC* (*Otis & Co.*), 142 F. 2d 411 (C. C. A. 3, 1944), the same Court, citing its former decision, again held that the hearing in the District Court under Section 11(e) is not a summary proceeding and that "any person affected by the plan shall have the right to be heard as to whether or not the plan is fair and equitable and appropriate to effectuate the provisions of Section 11" (p. 422). The Court stated further:

> "Moreover, the fact that notice is to be given to the persons affected by the plan shows that the theory of submission to the District Court is substantially similar to that required in respect to plan made pursuant to the provisions of Section 77B, or Chapter X of the Bankruptcy Act" (p. 422).

In *Okin* v. *S. E. C.*, 145 F. 2d 206 (C. C. A. 2, 1944),[1] and again in *Lowensbury* v. *S. E. C.*, 151 F. 2d 217 (C. C. A. 3, 1945), the courts upheld the contentions of the Commission that orders approving plans under Section 11(e), conditioned upon District Court approval (as was the plan in the instant case), are not reviewable by the Court of Appeals under Section 24(a) of the Act because such orders are "merely interlocutory". In the *Okin* case, the Second Circuit concluded that the legislative history of the Act evinced "a congressional intent that the relationship of the Securities and Exchange Commission and the District Court provided for in Section 11, should be 'exactly' the same as that of the Interstate Commerce Commission and the District Court in railroad reorganization under Section 77 of the Bankruptcy Act" (p. 208). And in the *Lowensbury* case, the Third Circuit quoted with approval the above expression and followed the holding of that case.

The opinion of the Court below refers to *Lahti* v. *New England Power Association*, 160 F. 2d 845, 858 (C. C. A. 1, 1947), and *Massachusetts Mutual Life Insurance Co.* v. *S. E. C.*, 151 F. 2d 424, 430 (C. C. A. 8, 1945), as "cases which look the other way, and [which] are entitled to great consideration" (R. 31). We suggest that the Court below was perhaps overstating the effect of those cases. In both of those cases the Court of Appeals was reviewing the decision of a District Court which had *approved* the findings of the Commission, and therefore what the appellate courts said had reference

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[1] Remanded on another point, 325 U. S. 840 (1945).

to *concurrent* findings of the Commission and the District Court. Thus, in the *Lahti* case, the Court said:

> "Upon full consideration, within the limited scope of our review, we have concluded that we must accept the judgment of the Commission and of the District Court on this matter" (p. 858).

Neither Court was required to consider the situation where the District Court had disagreed with the conclusion of the Commission that a plan submitted under Section 11(e) was "fair and equitable", and neither Court gave any indication that it would feel itself bound in such case to accept the judgment of the Commission and to reject the judgment of the District Court.

Petitioners rely principally upon *S. E. C.* v. *Chenery Corporation*, 332 U. S. 194. The holding of the Court below that the *Chenery* decision "cannot be deemed to be controlling in the case at bar" (R. 33) is, we submit, indisputably correct. This Court had before it for review a decision of the Court of Appeals of the District of Columbia reviewing an order of the Commission under Section 24(a) of the Act. That section contains the express injunction that "the findings of the Commission as to facts, if supported by substantial evidence, shall be conclusive", a provision which is not found in Section 11(e). This Court in the *Chenery* case was not called upon to consider and did not purport to decide the extent of the powers of a District Court acting under Section 11(e). Moreover, this Court was dealing with an order of the Commission which it considered to be within the administrative discretion entrusted by Congress to the Commission, "a judgment based upon public policy,

a judgment which Congress has indicated is of the type for the Commission to make * * * [a] conclusion [which] rests squarely in that area where administrative judgments are entitled to the greatest amount of weight by appellate courts. * * * the type of judgment which administrative agencies are best equipped to make and which justifies the use of the administrative process" (332 U. S. at p. 209). The reasoning of the second *Chenery* decision is consistent with the decisions of this Court under Section 77 of the Bankruptcy Act which emphasize that determinations upon questions wherein the public interest is paramount, are committed by Congress to the jurisdiction of the Interstate Commerce Commission,[1] but which accord to the District Court independent power in the fields where predominantly private interests are at stake.[2]

The "anomalous consequences" which the Commission suggests would flow if the construction of the powers of the District Court as laid down in this case should prevail[3] are, we believe, mere figments of imagination. Section 24(a) and Section 11(e) are not, as the Commission suggests, "alternative ways of submitting to judicial scrutiny a plan theretofore approved by the Commission"; the Commission itself has contended, and the lower

[1] E.g., *Ecker v. Western Pacific R. Corp.*, 318 U. S. 448, 468 (1943):

> "When the public interest, as distinguished from private, bulks large in the problem, the solution is largely a function of the legislative and administrative agencies of government with their facilities and experience in investigating all aspects of the problem and appraising the general interest."

[2] *Id.* at p. 479.

[3] Commission's Petition for Certiorari, No. 226, pp. 23-24.

courts have uniformly held, that an order like the one here made by the Commission can only be presented to the District Court under Section 11(e) and cannot be reviewed by the Court of Appeals under Section 24(a) prior to the action of the District Court thereon.[1] In recognition of the fact that the statutory scheme renders inapplicable the general review provisions of Section 24(a) with respect to Section 11(e) plans cutting across stockholders' charter rights, the Commission has established the practice of expressly conditioning its approval of such plans upon District Court enforcement.[2] It follows that the two anomalies suggested by the Commission, namely, alternative applications to the District Court and the Court of Appeals or an application to the District Court for enforcement after affirmance of the Commission's order by the Court of Appeals, could not arise.

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[1] *Okin* v. *S. E. C.*, 145 F. 2d 206 (C. C. A. 2, 1944); *Lowensbury* v. *S. E. C.*, 151 F. 2d 217 (C. C. A. 3, 1945), cert. den. 326 U. S. 782.

[2] Cf. statement of Judge Goodrich in the *Lowensbury* decision, *supra*, at p. 218.

Petitioners attempt to argue that special weight is attributable to the Commission's approval of a plan because District Court enforcement is optional with the company, is also devoid of merit. Some plans do not "affect" stockholders' rights because they are carried out strictly in accordance with charter provisions or pursuant to vote of the stockholders in accordance with the provisions of state statutes. Cf. *Northern New England Company*, Holding Company Act Release No. 8401 (1948) at p. 4. But where the plan cuts across charter rights, District Court approval and enforcement is essential, as the Commission has recognized:

> "In some cases where Section 11(e) plans have been approved by the Commission, the companies are unable to carry them out without obtaining a court order. The Act permits the Commission at the request of the companies to go to court for the purpose of obtaining enforcement of such plans. * * *
> * * * As has been said, security holders are not required to accept Section 11(e) plans unless they are found fair and equitable by both the Commission and a United States District Court." (Tenth Annual Report of the Securities and Exchange Commission, p. 66.)

The fear expressed by the Commission that the conferring of discretion on the District Court "would preclude uniform administration of the statute and make the treatment of nationwide groups of security holders depend upon accidents of venue," would, if warranted, be an argument for amending the statute rather than for not enforcing the statute as written. Congress has evidenced a clear intention that the district courts shall exercise an independent judgment in determining whether public utility holding company reorganization plans are "fair and equitable". Indeed, as has been shown, *supra*, pp. 134-5, Congress placed great reliance on the use of the techniques which the *Courts* had employed in carrying out dissolutions under the anti-trust statutes and in equity reorganizations; and had received positive assurance that "there is really a double check on the plan and final determination rests as in the past in the courts".

Like power is exercised by district courts in equity reorganizations, in corporate bankruptcies under Chapter X, and in railroad bankruptcies under Section 77, without untoward consequences to nationwide groups of security holders, and we see no reason why security holders of utility holding companies should be required to look only to the Commission for protection and should be deprived of the benefit of an independent judicial judgment, particularly when it is remembered that *this statute is the only reorganization statute which does not accord to security holders the right to vote upon a reorganization plan.*

The final fear expressed by the Commission, that a vesting of discretion in the District Court to check the Commission would lead to "a possibility of deadlock re-

sulting from conscientious disagreement", is also unfounded, judging from the experience of the district courts and the Interstate Commerce Commission in the administration of Section 77 of the Bankruptcy Act. Under that statute, as this Court has said, the judicial process "is, as it were, brigaded with the administrative process of the Commission".[1] "These reorganizations may be attained only through properly co-ordinated action between the Commission and the Court."[2] In the absence of evidence that the Commission and the courts are engaged in an irreconcilable conflict, this Court will not assume that such a situation will arise. Experience, both before[3] and since[4] the decision of the Court below, does not sug-

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[1] *Palmer* v. *Massachusetts*, 308 U. S. 79, 87 (1939).

[2] *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448, 475 (1943).

[3] The Court below refers to the fact that the Commission had submitted some sixty-three Section 11(e) plans to the District Courts for enforcement, all of which have been carried out, and that Judge Leahy had passed upon twenty-seven of those plans (R. 30, 39). Prior to the *Engineers* decision, in fulfilling his "independent duty" Judge Leahy had concurred in the conclusions of the Commission in every plan presented to him with the sole exception of a single phase of one plan. The Third Circuit reversed, holding that since the question related to the "appropriateness" of the "particular remedial measures" required to effectuate Section 11(b), the Commission's judgment should prevail (*In re Standard Gas & Electric Co.*, 151 F. 2d 326, 331). However, subsequent events established the correctness of the District Judge's fears that fluctuating markets would render the plan unfair; and as a result the Commission itself concurred in the view that the claims of the senior security holders should be discharged in cash. (See *In re Standard Gas & Electric Co.*, 63 F. Supp. 876.)

[4] Subsequent to the Circuit Court's decision in the instant case Judge Leahy has passed on some nine additional Section 11(e) plans, all of which he has approved and enforced.

The beneficial effect of the decision in the instant case in its practical operation is evidenced by the recent decision of the District Court of Minnesota, *In the Matter of Northern States Power Company*, 80 F. Supp. 193 (N. D. Minn., 1948). Holding that the Circuit

gest that the district courts will endeavor to encroach upon the rightful province of the Commission; if anything, the tendency of the courts is all the other way.

VIII. There is no valid basis for remanding this case to the Commission.

The only valid grounds upon which a remand of this case to the Commission can be predicated are either that as a formal matter, even though $100 per share is the most the preferred stockholders may lawfully receive, the Commission must approve the payment to them of $100 (instead of $100 plus premiums) before that portion of the plan can be enforced; or that as a substantive matter the Commission could, on this record and on a proper rationale, lawfully authorize the payment to the preferred of more than $100 per share. Neither ground is here present. As a formal matter, the Commission has already given its approval to the payment of only $100 per share to the preferred if it be decided that this sum is all that the "fair and equitable" standard authorizes. As a substantive matter, $100 per share is the most that "fair and equitable" treatment permits the preferred stockholders to receive.

Court's decision in the *Engineers* case did not preclude him from attaching great weight to the Commission's determination as to earning power and allocation, the District Judge fully upheld them; but only after making a careful check of their correctness in the exercise of his "independent duty". The same course was followed, and the same result was reached, by the District Court of Maine, *In the Matter of American & Foreign Power Company*, 80 F. Supp. 514, 523 (S. D. Maine, 1948).

The fact is that there has not been a single instance of a refusal by a District Court to approve and enforce a Section 11(e) plan, or any portion thereof, since the decision in the instant case, although more than twelve such plans have been passed on by the Courts.

A. Procedural Aspects

What this Court has said as to the importance of expedition, through coordinated procedure between the District Court and the Commission in reorganizations under Section 77 of the Bankruptcy Act, is equally applicable here:

> "Not only are those who institute the proceeding and those who carry it forward bound to exercise the highest degree of diligence, but it is the duty of the Court and of the Interstate Commerce Commission to see that they do. Proceedings of this character, involving public and private interests of such magnitude, should, so far as practicable, be given the right of way both by the Court and the Commission to the end that they may be speedily determined." [1]

And in *Ecker v. Western Pacific R.R. Co.*, 318 U. S. 448, the Court stated (p. 475): "These reorganizations may be attained only through properly coordinated action between the Commission and the Court". The Court of Appeals' requirement for remand negates precisely such a coordinated procedure as was employed in this case.

The Commission in requiring the plan to be amended so as to pay premiums, over the objections of the company and the common stockholders, was necessarily aware that there existed no judicial sanction whatever for such premium payments, and that, on the contrary, the Commission itself and numerous Courts, including four different Circuit Courts of Appeals, had consistently and uniformly held over a period of five years that pay-

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[1] *Continental Illinois Bank v. C. R. I. & P. Ry. Co.*, 294 U. S. 648, 685. See also *Insurance Group v. Denver & Rio Grande W. R. Co.*, 329 U. S. 607, 612. Cf. *Federal Trade Commission v. Curtis Co.*, 260 U. S. 568, 580; *International Shoe Company v. Federal Trade Commission*, 280 U. S. 291, 297.

ment of premiums to senior security holders at the expense of the junior holders could not be required in reorganizations or liquidations under Section 11(e) of the Act in consonance with the "fair and equitable standard" of Section 11(e).[1]

Hence, in an effort to secure the expeditious execution of those portions of the plan which were separable and approved, and to avoid resubmission of the plan to the Commission if such resubmission served only the formality of having the Commission give its approval to a result which the law required, the Commission amended its order in this proceeding (R. 165a-174a). By the amendments the Commission provided for the parties to enter into an escrow arrangement under which the depositary is to pay over to Engineers the principal and interest deposited in escrow "Upon delivery * * * of an opinion of independent counsel * * * accompanied by a certified copy of the order or decree involved, to the effect that * * * an order or decree of any court having jurisdiction, has been entered, has become final and is no longer subject to appeal, which * * * court order or decree determines or finds that the holders of Preferred Stock are not entitled to receive any amounts in addition to the amount of $100 per share plus accrued dividends * * *" (R. 328a).

Underlying this escrow agreement is an important consideration of which the Commission doubtless was aware. If the plan were executed in all respects but that under dispute, $100 per share would be distributed to each preferred stockholder. It would then be impossible as a practical matter for the common stockholders to recover any amounts by which the $100 might subsequently be found to be in excess of "fair and equitable" treatment

[1] *Supra*, p. 55, notes 3 and 4.

for the preferred. It is in the light of its inability to accord the common stockholders "fair and equitable" treatment if such treatment should require the Commission, upon re-examining the rights of the parties, to award the preferred less than $100 per share, that the Commission informed the Court below: " * * * the Commission has already contingently approved an alternative allocation of cash to the preferred stockholders at the amount of the liquidation preference if as a result of the processes of review in the District Court and on appeal therefrom this should be judicially determined fair and equitable." [1]

It is thus apparent that the Commission had given its prior consideration and advance approval to the plan in the form approved and enforced by the District Court's order of May 29, 1947 (R. 318a); and indeed the record discloses that this order was actually drafted and submitted to the District Court for signature by the Commission's attorneys (R. 357a). These circumstances scarcely justify the Court of Appeals' statement that the District Court erred in entering an order approving and enforcing the plan as amended *by it*,[2] and without the Commission's prior consideration and approval.

On the contrary, the procedure followed by the District Court in every particular was that which the Com-

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[1] R. 44, n. 1, Commission's petition for rehearing in the Circuit Court.

[2] "The Court below, therefore, erred in one particular: *It entered an order approving and enforcing the plan as amended by it.* It was without power to do this. The provisions of Section 11(e) make it clear that the Commission in the first instance must approve the plan and find it to be fair and equitable. If, as here, the district court disagrees with the conclusion of the Commission that the plan is fair and equitable, it must refuse to approve the plan and 'remand' the record to the Commission for further and appropriate action by it" (R. 39). (Emphasis supplied.)

mission in its opinions and orders and by its attorneys in open court[1] requested and urged the Court to follow, including establishment of the escrow fund and non-remand of the proceedings to the Commission by reason of the Court's disapproval of the premium payments. Although concededly these circumstances do not insulate the District Court's decree from attack if the Commission's actions were in effect "ultra vires", we submit that they do completely refute any suggestion that the Court engaged in a process of amending the plan in respects which procedurally, at least had not received the full concurrence and approval of the Commission, and, indeed, as to which the Commission had not actually been the prime mover.

Nor do we think the procedure urged upon the Court by the Commission can properly be deemed "ultra vires". If the Courts did not find the Commission's new "investment value ex the Act" doctrine consonant with established legal principles and the statutory intent, nothing further remained to be decided; for in such event the preferred holders would necessarily receive payment of only $100 per share plus dividends, in conformance with a long line of Commission and Court decisions. Accordingly, the Commission correctly recognized that the basic issue was one of legal and statutory interpretation, as to which the last word was not in the Commission but in the Courts.[2]

Therefore, in approving as fair and equitable payment of only the liquidation preference in the event the District Court held payment of the premiums unfair and inequi-

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[1] R. 257a-260a, 281a-282a.

[2] If confirmation be needed for this provision, it is amply furnished by the legislative history of the statute, to which reference was made in the Court of Appeals' opinion (R. 22, 23).

table (and such determination became final for lack of appeal or were affirmed upon appeal), it is evident the Commission was not "waiving" or "rejecting" its statutory role, but was performing it in the only way consonant with reason and the repeated admonitions of this Court for expeditious and coordinated procedure in reorganizations of this character.[1]

Accordingly, unless it is held that the Commission, on a reconsideration, could lawfully award more than $100 plus accrued dividends to the preferred stockholders, formal correctness does not require resubmitting this case to the Commission.

B. Substantive Aspects

We submit that, as we have shown, the Commission may not, on any valid basis, award the preferred stockholders more than the $100 plus accrued dividends which they have already received.

Thus, if the present liquidation comes within the charter provisions, the "fair and equitable" standard limits the preferred stockholders to receipt of no more than the terms of the corporate charter authorize, i.e., $100 per share plus accrued dividends. The same conclusion follows even if the present liquidation is deemed not to come within the terms of the corporate charter, since the judicially approved and correct interpretation of the "fair and equitable" standard precludes the payment of pre-

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[1] See p. 149, *supra*. Cf. *Comstock* v. *Group of Investors*, 335 U. S. 211; majority opinion pp. 227-228, minority p. 236.

Rejection of the coordinated procedure followed in the instant case would also entail a special financial burden for the common stockholders. Under the Commission's decision, they are required to bear the entire expense of all phases of the proceedings and the litigation (R. 72a-82a).

miums on preferred stocks which are retired under compulsion of the Act, where holders are paid out in cash and freed from the risks of a new enterprise.

Decision of this case on either of the foregoing grounds would make remand to the Commission obviously unnecessary. However, if the question upon which this case is made to turn is whether the "equitable equivalent" of the rights surrendered by the preferred stockholders is more than $100 per share, the only possible answer is in the negative; and since the District Court so found, upon consideration of the very factors which the Court of Appeals held must be considered, there is no valid basis for remanding the case to the Commission.

Both the District Court and the Court of Appeals agreed that the Commission had erroneously determined the "equitable equivalent" of the rights which the preferred stockholders were here giving up. The Court of Appeals concluded, however, that the District Court had substituted its "valuations" of the "equitable equivalents" for those of the Commission and that it was powerless to do so. Accordingly, it directed the case to be remanded to the Commission. In essence, this conclusion reduces itself to a contention that the District Judge should have worded only negatively what he also worded affirmatively; that he should have held the provision for the payment of premiums "unfair and inequitable" but should not have found affirmatively that the preferred stockholders received "fair and equitable" treatment upon the receipt of only $100 per share plus dividends.

We may assume, without conceding, that had the District Court in fact substituted its "valuations" for those of the Commission and decided, for example, that the "equitable equivalent" of the rights surrendered by the

preferred stockholders was $70 per share, it would have acted beyond its authority. But that is not the case here. The District Court did not make any such "valuation" of the "equitable equivalent" of the rights surrendered by the preferred stock or substitute any "valuation of its own" for that of the Commission.

What the District Court "valued" was not the preferred stocks but the Commission's "investment value ex the Act" doctrine. In deciding that this doctrine had no warrant in the statute or settled legal principles, it necessarily examined all the factors in this record which could be deemed relevant under any standards recognized in the statute and judicial decisions, and concluded that the "equitable equivalent" of the rights surrendered by the preferred stockholders could not exceed $100. We have shown that an examination of these factors can lead to no other conclusion. Accordingly, we submit that if the District Court had the authority to examine these relevant factors there is no valid basis for remand of this case to the Commission.

It is not necessary to explore the full breadth of the powers of the District Court in order to uphold the exercise of its authority here. The District Judge did not determine that the Commission must award a specific sum to the preferred stockholders; nor has it ruled that while the Commission might fairly and equitably award more than $100 to the preferred, a maximum of $100 was also "fair and equitable" and in its judgment sufficient. In either of those cases it might be contended that the District Court was intruding upon the Commission's legitimate function under the Act. But here the Court has decided only that the Commission could not

lawfully award more than $100; i.e., it has examined the record made before the Commission in order to determine the outer limits of permissible Commission action on that record, and concluded that no more than $100 can "fairly and equitably" be paid to the preferreds.

The District Court's power thus to appraise the Commission's action was plainly within the delegation of jurisdiction contained in Section 11(e). Under that section, as we have shown, the District Court is not a mere "review court". It has all the "extraordinary powers" it has "been accustomed to exercise when called upon under the Sherman and Hepburn Act to effect compulsory corporate readjustments" [1]—the plenary powers of a court of equity. The statute imposed upon the District Judge the "independent duty" [2] to satisfy himself that the plan here submitted was "fair and equitable". We need not insist that in "the realm of judgment",[3] which is governed by the "fair and equitable" standard, the District Court's judgment rather than the Commission's should furnish the "final determination" of what is "fair and equitable".[4] In any case, under the narrowest view, the

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[1] Senate Report No. 621, accompanying S. 2796, 74th Cong., First Session, pp. 13 and 14, quoted *supra*, p. 134.

[2] Cf. statements of the Commission's representatives before the Congressional Committee considering amendments to the Act (*supra*, pp. 136-7), as well as the statement of Commission Counsel before the District Court in the instant case (*supra*, p. 138).

[3] "Since such a determination rests in the realm of judgment rather than mathematics, there is an area for disagreement. But we are not performing the functions of the District Court under § 77(e)." *Group of Investors* v. *Milwaukee R. Co.*, 318 U. S. 523, 564; quoted *supra* at p. 132.

[4] Cf. statement of Senator Wheeler (*supra*, p. 135) "* * * there is really a double check upon the plan, and final determination rests as in the past in the courts".

District Court's "extraordinary powers" embrace the authority at least to examine the record made before the Commission and to determine the outer limits of permissible Commission action under the "fair and equitable" standard.

Accordingly, we submit that the Court of Appeals erred in ordering the case to be remanded to the Commission. Since the District Court had the authority to make the "careful and far-reaching examination of the relevant factors" which the Court of Appeals found it made, and properly concluded that the preferred stockholders could not lawfully receive more than $100 per share, there is no function left for the Commission here except formally to approve the payment of $100 to the preferred. This function, as we have shown, it has performed in approving the escrow arrangement.

CONCLUSION

The judgment of the Court below should be vacated with directions to enter an order affirming the decree of the District Court.

Dated, December 20, 1948.

Respectfully submitted,

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APPENDIX A

Pertinent Provisions of the Public Utility Holding Company Act of 1935

SIMPLIFICATION OF HOLDING-COMPANY SYSTEMS

Sec. 11. (a) It shall be the duty of the Commission to examine the corporate structure of every registered holding company and subsidiary company thereof, the relationships among the companies in the holding-company system of every such company and the character of the interests thereof and the properties owned or controlled thereby to determine the extent to which the corporate structure of such holding-company system and the companies therein may be simplified, unnecessary complexities therein eliminated, voting power fairly and equitably distributed among the holders of securities thereof, and the properties and business thereof confined to those necessary or appropriate to the operations of an integrated public-utility system.

(b) It shall be the duty of the Commission, as soon as practicable after January 1, 1938:

(1) To require by order, after notice and opportunity for hearing, that each registered holding company, and each subsidiary company thereof, shall take such action as the Commission shall find necessary to limit the operations of the holding-company system of which such company is a part to a single integrated public-utility system, and to such other businesses as are reasonably incidental, or economically necessary or appropriate to the operations of such integrated public-utility system: *Provided, however,* That the Commission shall permit a registered holding company to continue to control one or more additional integrated public-utility systems, if, after notice and opportunity for hearing, it finds that—

(A) Each of such additional systems cannot be operated as an independent system without the loss of substantial economies which can be secured by the retention of control by such holding company of such system;

(B) All of such additional systems are located in one State, or in adjoining States, or in a contiguous foreign country; and

(C) The continued combination of such systems under the control of such holding company is not so large (considering the state of the art and the area or region affected) as to impair the advantages of localized management, efficient operation, or the effectiveness of regulation.

The Commission may permit as reasonably incidental, or economically necessary or appropriate to the operations of one or more integrated public-utility systems the retention of an interest in any business (other than the business of a public-utility company as such) which the Commission shall find necessary or appropriate in the public interest or for the protection of investors or consumers and not detrimental to the proper functioning of such system or systems.

(2) To require by order, after notice and opportunity for hearing, that each registered holding company, and each subsidiary company thereof, shall take such steps as the Commission shall find necessary to ensure that the corporate structure or continued existence of any company in the holding-company system does not unduly or unnecessarily complicate the structure, or unfairly or inequitably distribute voting power among security holders, of such holding-company system. In carrying out the provisions of this paragraph the Commission shall require each registered holding company (and any company in the

same holding-company system with such holding company) to take such action as the Commission shall find necessary in order that such holding company shall cease to be a holding company with respect to each of its subsidiary companies which itself has a subsidiary company which is a holding company. Except for the purpose of fairly and equitably distributing voting power among the security holders of such company, nothing in this paragraph shall authorize the Commission to require any change in the corporate structure or existence of any company which is not a holding company, or of any company whose principal business is that of a public-utility company.

The Commission may by order revoke or modify any order previously made under this subsection, if, after notice and opportunity for hearing, it finds that the conditions upon which the order was predicated do not exist. Any order made under this subsection shall be subject to judicial review as provided in section 24.

(c) Any order under subsection (b) shall be complied with within one year from the date of such order; but the Commission shall, upon a showing (made before or after the entry of such order) that the applicant has been or will be unable in the exercise of due diligence to comply with such order within such time, extend such time for an additional period not exceeding one year if it finds such extension necessary or appropriate in the public interest or for the protection of investors or consumers.

(d) The Commission may apply to a court, in accordance with the provisions of subsection (f) of section 18, to enforce compliance with any order issued under subsection (b). In any such proceeding, the court as a court of equity may, to such extent as it deems necessary for purposes of enforcement of such order, take exclusive jurisdiction and possession of the company or companies and

the assets thereof, wherever located; and the court shall have jurisdiction, in any such proceeding, to appoint a trustee, and the court may constitute and appoint the Commission as sole trustee, to hold or administer under the direction of the court the assets so possessed. In any proceeding for the enforcement of an order of the Commission issued under subsection (b), the trustee with the approval of the court shall have power to dispose of any or all of such assets and, subject to such terms and conditions as the court may prescribe, may make such disposition in accordance with a fair and equitable reorganization plan which shall have been approved by the Commission after opportunity for hearing. Such reorganization plan may be proposed in the first instance by the Commission, or, subject to such rules and regulations as the Commission may deem necessary or appropriate in the public interest or for the protection of investors, by any person having a bona fide interest (as defined by the rules and regulations of the Commission) in the reorganization.

(e) In accordance with such rules and regulations or order as the Commission may deem necessary or appropriate in the public interest or for the protection of investors or consumers, any registered holding company or any subsidiary company of a registered holding company may, at any time after January 1, 1936, submit a plan to the Commission for the divestment of control, securities, or other assets, or for other action by such company or any subsidiary company thereof for the purpose of enabling such company or any subsidiary company thereof to comply with the provisions of subsection (b). If, after notice and opportunity for hearing, the Commission shall find such plan, as submitted or as modified, necessary to effectuate the provisions of subsection (b) and fair and equitable to the persons affected by such plan, the Commission shall make an order approving such plan; and the Commission, at the request of the company, may apply to a court, in accordance with the provisions of sub-

section (f) of section 18, to enforce and carry out the terms and provisions of such plan. If, upon any such application, the court, after notice and opportunity for hearing, shall approve such plan as fair and equitable and as appropriate to effectuate the provisions of section 11, the court as a court of equity may, to such extent as it deems necessary for the purpose of carrying out the terms and provisions of such plan, take exclusive jurisdiction and possession of the company or companies and the assets thereof, wherever located; and the court shall have jurisdiction to appoint a trustee, and the court may constitute and appoint the Commission as sole trustee, to hold or administer, under the direction of the court and in accordance with the plan theretofore approved by the court and the Commission, the assets so possessed.

(f) In any proceeding in a court of the United States, whether under this section or otherwise, in which a receiver or trustee is appointed for any registered holding company, or any subsidiary company thereof, the court may constitute and appoint the Commission as sole trustee or receiver, subject to the directions and orders of the court, whether or not a trustee or receiver shall theretofore have been appointed, and in any such proceeding the court shall not appoint any person other than the Commission as trustee or receiver without notifying the Commission and giving it an opportunity to be heard before making any such appointment. In no proceeding under this section or otherwise shall the Commission be appointed as trustee or receiver without its express consent. In any such proceeding a reorganization plan for a registered holding company or any subsidiary company thereof shall not become effective unless such plan shall have been approved by the Commission after opportunity for hearing prior to its submission to the court. Notwithstanding any other provision of law, any such reorganization plan may be proposed in the first instance by the Commission or, subject to such rules and regulations as the Commission

may deem necessary or appropriate in the public interest or for the protection of investors, by any person having a bona fide interest (as defined by the rules and regulations of the Commission) in the reorganization. The Commission may, by such rules and regulations or order as it may deem necessary or appropriate in the public interest or for the protection of investors or consumers, require that any or all fees, expense, and remuneration, to whomsoever paid, in connection with any reorganization, dissolution, liquidation, bankruptcy, or receivership of a registered holding company or subsidiary company thereof, in any such proceeding, shall be subject to approval by the Commission.

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COURT REVIEW OF ORDERS

Sec. 24. (a) Any person or party aggrieved by an order issued by the Commission under this title may obtain a review of such order in the circuit court of appeals of the United States within any circuit wherein such person resides or has his principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the entry of such order, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall be forthwith served upon any member of the Commission, or upon any officer thereof designated by the Commission for that purpose, and thereupon the Commission shall certify and file in the court a transcript of the record upon which the order complained of was entered. Upon the filing of such transcript such court shall have exclusive jurisdiction to affirm, modify, or set aside such order, in whole or in part. No objection to the order of the Commission shall

be considered by the court unless such objection shall have been urged before the Commission or unless there were reasonable grounds for failure so to do. The findings of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If application is made to the court for leave to adduce additional evidence, and it is shown to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceeding before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which, if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court affirming, modifying, or setting aside, in whole or in part, any such order of the Commission shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 346 and 347).

APPENDIX B

Excerpts from the Certificate of Incorporation of Engineers Public Service Company

The Certificate of Incorporation of Engineers provided in pertinent part as follows:

"III. *Preference on Liquidation* etc.[1] In the event of any liquidation, dissolution or winding up of this Corporation, or any reduction of its capital stock resulting in any distribution of its assets to its stockholders, the holders of the preferred stock of each series shall be entitled to receive, for each share thereof, an amount equal to $100, together with all dividends accrued or in arrears thereon, plus, in case such liquidation, dissolution or winding up or reduction shall have been voluntary, the fixed redemption premium for such series, if any, before any distribution of the assets shall be made to the holders of the common stock; but the holders of the preferred stock shall be entitled to no further participation in such distribution. * * *"

"IV. *Redemption and Repurchase.*[2] The Corporation may, at its option, at any time or from time to time redeem the whole or any part of the preferred stock or of any series thereof, at a price for each share thereof equal to $100, plus the fixed redemption premium therefor, if any, together with the amount of any dividends accrued or in arrears thereon. * * *"[3]

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[1] Engineers' Ex. No. 33, R. 1412a.

[2] Engineers' Ex. No. 33, R. 1413a.

[3] By resolutions of the Board of Directors, the fixed redemption premium of the $5 series was fixed at $10 per share for shares redeemed on or before June 30, 1938, and $5 per share for shares redeemed thereafter (R. 1428a). The fixed redemption premiums of the $5.50 and $6 series was fixed at $10 per share (R. 1430a-1431a).

"This Corporation may also from time to time repurchase shares of its preferred stock at not exceeding the price or prices at which the same may be redeemed. * * *"

* * * * * *

"Division B—The Common Stock[1]

II. *Distribution of Assets.* In the event of any liquidation, dissolution or winding up of this Corporation, or any reduction of its capital stock, resultin any distribution of its assets to its stockholders, after there shall have been paid to or set aside for the holders of the preferred stock the full preferential amounts to which they are respectively entitled under the provisions of Paragraph III of Division A of this Article Fourth, the holders of the common stock shall be entitled to receive, *pro rata,* all of the remaining assets of this Corporation available for distribution to its stockholders."

[1] Engineers' Ex. 33, R. 1417a.

APPENDIX C

Excerpts from Typical News Stories Appearing in the Press About the Time the Charter of Engineers Was Being Drafted and the Preferred Stocks Offered for Sale *

From the New York Times, December 30, 1924

ASKS "POWER TRUST" INQUIRY.

NORRIS'S NEW MUSCLE SHOALS MOVE HELD UP BY EDGE.

WASHINGTON, Dec. 29.—The Federal Trade Commission would be directed to investigate an alleged "power trust" under a resolution introduced in the Senate today by Chairman Norris of the Agriculture Committee.

His proposal was incidental to the bitter Congressional fight over Muscle Shoals, during which it has been charged on the Senate floor that a combination of power interests was seeking to dictate the Government's final decision. Senator Norris has been active in opposing the Underwood bill for Government ownership of the Muscle Shoals property, with a provision for its lease to private concerns.

Mr. Norris asked for immediate consideration of his resolution, but Senator Edge, Republican, New Jersey, objected, and it went over for one day under the rules.

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* This material relates to the discussion at pages 41-43, *supra*, and is submitted as further documentation of our contention that the preferred and common stockholders of *Engineers* could not have been unmindful of the possibility that some form of future governmental action directed against utility holding companies might bring into play the liquidation provisions of the charter.

The charter of *Engineers* was filed and recorded June 23, 1925. The $5 and $5.50 series of preferred stocks were initially offered to the public in March and October of 1928, and the $6 preferred in September, 1930.

The resolution would require an investigation into the ownership of stocks and bonds and the directorates of power companies, and into the interest of manufacturers of electrical supplies, banks and trust companies in the business. The President would be requested to give the investigating committee access to official Treasury records bearing on the subject.

Senator Edge declared that such a far-reaching resolution should not be considered hastily. He said "millions of dollars" would be required to conduct such an inquiry.

From the New York Times, December 31, 1924 *

GENERAL ELECTRIC GIVES UP HOLDINGS IN PUBLIC UTILITIES

RELINQUISHES ELECTRIC BOND AND SHARE COMPANY, CONTROLLING 100 POWER ENTERPRISES.

WALL STREET SURPRISED

NEWS SENDS STOCK UP TO NEW HIGH OF 307⅜, BUT HEAVY SELLING CLOSES IT AT 297.

NEW COMPANY ANNOUNCED

TO TAKE OVER GENERAL ELECTRIC INTEREST AND DISTRIBUTE ITS SHARES TO GENERAL ELECTRIC STOCKHOLDERS

Directors of the General Electric Company announced yester-

NORRIS TO PRESS INQUIRY.

GENERAL ELECTRIC ACTION WON'T HALT POWER RESOLUTION.

Special to The New York Times.

WASHINGTON, Dec. 30—Withdrawal of the General Electric Company from public utility ownership will not deter Senator Norris of Nebraska from pushing his resolution providing for an investigation of the so-called power trust. While General Electric is a part of the alleged trust, Mr. Norris and those who agree with him take the position that it is the duty of the Senate to make an inquiry to determine what influences have been at work in behalf of private operation of Muscle Shoals and other similar

* No sooner had the Senate authorized the first Federal Trade investigation of public utility Holding Companies than it was announced that General Electric Company would divest itself of control of the gigantic Electric Bond and Share system. (Cf. *Electric Bond and Share Co. et al.*, 11 S. E. C. 1146, 1163.)

day half an hour before the closing of the Stock Exchange that it would dispose of its holdings in the Electric Bond and Share Company, the common stock of which it owns entirely. The decision of General Electric to separate the public utility end of its business from the manufacturing end was distinctly a surprise to Wall Street, and General Electric stock, which had risen 100 points within the year, advanced sharply to a new high point of 307⅜. Some uncertainty developed as to the possible effect of the retirement of General Electric from the public utility field, and selling carried the quotation down to 296, closing at 297, a net loss for the day of 2⅞.

* * *

projects throughout the country.

Senator La Follette is in sympathy with Mr. Norris' proposal to examine persons who are supposed to have a knowledge of the activities of the power "trust." The Third Party platform, upon which Mr. La Follette ran as a candidate for President in the late election, contained a declaration on the subject of the development of power.

It recommended a policy of Government ownership, stating that Government ownership in Canada had resulted in lower service rates, much lower, it was stated, than provided by private corporations in the United States.

While Senator Norris did not support the Third Party movement, it is known that he is in accord with the views of Mr. La Follette, favorable to the adoption of a Government ownership policy in the handling of all potential water sites to which the Federal Government holds title. The indications are that Senator Norris will press his resolution with a view to making the investigation he has in mind the basis of a Government ownership bill.

From the New York Times, February 18, 1925

PINCHOT FOR CURB OF POWER MONOPOLY

SENDS SURVEY REPORT TO LEGISLATURE, STRESSING THE NEED OF REGULATION.

NOVEL PROPOSALS MADE

BASIC FEATURE IS PLAN TO MAKE RANSMISSION LINES COMMON CARRIERS.

POWER EXPORT UNDER BAN

REPORT, COMPRISING 500 PAGES, IS CALLED GREATEST POWER SURVEY EVER MADE

HARRISBURG, Feb. 17.—with a declaration that the electric utilities are a gigantic monopoly without parallel, Governor Pinchot told the Legislature today that "the question is whether we shall regulate it or whether it shall regulate us." He made this statement in presenting the report of the Giant Power Survey Board, embodying the facts of a comprehensive survey, authorized by the last Legislature. With the report were presented fifteen bills designed to carry out the recommendations that are made.

* * * * * * *

The Federal Trade Commission Investigation, Which Culminated in Adoption of the Public Utility Holding Company Act, Was in Full Swing by the Time the Preferred Stocks of Engineers Were Being Offered to the Public

From the New York Times, February 16, 1928

SENATE VOTES, 46-31, FOR POWER INQUIRY BY THE TRADE BOARD

WALSH OF MONTANA, PRESSING FOR SENATE INVESTIGATION, IS BEATEN AFTER BITTER FIGHT.

HOT DEBATE FOR 9 HOURS

GLASS AND BRUCE IN SPIRITED CLASH WHEN THE LATTER ATTACKS MONTANAN.

HUNT FOR ELECTION FUNDS

VICTORIOUS GEORGE AMENDMENT AUTHORIZING COMMISSION TO DIG INTO CORPORATIONS' ACTIVITIES.

Special to The New York Times.

WASHINGTON, Feb. 15.—By a vote of 46 to 31, and over the desperate protest of Senator Walsh of Montana, the Senate tonight referred the proposed "power trust" investigation to the Federal Trade Commission instead of authorizing an inquiry by a special committee of five Senators as proposed by Mr. Walsh.

The final vote came at 9 o'clock tonight after a nine-hour session of acrimonious debate, marked by frequent clashes,

particularly between Senators Glass of Virginia and Bruce of Maryland. Senator Walsh of Montana, many of the Democrats and a large proportion of the Progressive Republicans tried to defeat the motion to hand the inquiry over to the Trade Commission, as proposed by Senator George of Georgia.

Hoping that delay might gain more votes in favor of a Senate investigation, Senator Walsh and his lieutenants endeavored three times to adjourn the Senate. They were defeated in increasingly decisive votes. Senator George and Senator Watson, Chairman of the Senate Interstate Commerce Committee, were willing to agree to give a specific time to vote, but Mr. Walsh refused to consent.

The outcome of the fight was in doubt until the vote was taken, although the advocates of the Trade Commission plan were gaining strength on the preliminary votes.

* * * * * *

On motion of Senator George, the Senate adopted an amendment directing the Trade Commission to ascertain whether any of the alleged practices referred to in the Walsh resolution "constitute unfair methods in commerce, tend to restraint of trade and commerce or to create a monopoly, or constitute a violation of the Federal anti-trust laws."

The purpose of this, Mr. George said, was to make certain that the commission would carry out the inquiry and make a proper report on the resolution.

The Senate also accepted an amendment by Senator Black of Alabama providing that the sessions of the commission during the investigation should be open to the public. * * *

* * * * * *

SENATOR GLASS ATTACKS BRUCE.

Tonight Mr. Glass accused Mr. Bruce of trying to block the Teapot Dome inquiry, "just as he is trying now", to send the "power trust" investigation to the Federal Trade

Commission. Mr. Glass accused Mr. Bruce of "defending Harry M. Daugherty in glowing language."

The two Senators shouted at each other at the same time, Senator Moses meanwhile banging his gavel. Above the uproar, Mr. Glass could be heard condemning Mr. Bruce for "unkind and vitriolic excoriations" of Mr. Walsh.

Mr. Moses called Mr. Bruce to order twice, but the Maryland man sat down, expressing regret to the Senate that he had seemed to lose his temper. He said he had never defended Harry M. Daugherty, although he had said he admired him for having the courage of his convictions.

The name of Governor Smith was brought into the debate again when Mr. Wheeler asked Mr. Copeland if the New York Governor had not tried to control the power trusts in his State.

* * * * * *

From the New York Times, July 3, 1928

SAYS UTILITIES PAID OFFICIAL IN OHIO

COMPANIES' AGENT QUOTED AS ASSERTING SECRETARY TOOK MONEY FOR SPEECHES.

TALK OF A $400,000 FUND

"POLITICAL" RESULTS WERE SOUGHT BY CONTRIBUTIONS OF 100 ORGANIZATIONS.

WASHINGTON, July 2 (AP).—Groundwork laid by public utility organizations to prevent "politicians" from conducting an investigation into the industry under the Walsh Senate resolution and widespread methods to influence public opinion by obtaining free publicity in newspapers were revealed today in the **Federal Trade Commission's utility inquiry.**

Documents from the office files of Arthur F. Herwig of Milwaukee, Director of the Wisconsin Public Utility Information Bureau, for the first time disclosed preparations made by the joint committee of National Utilities Associations last year for the proposed Walsh investigation and heretofore unrevealed publicity methods of Ohio utility organizations.

* * * * * *

The other outstanding development of today's hearing was a report of the meeting of public utility men in Atlantic City, in 1922, in which Ben E. Ling, director of the Ohio Information Bureau, was quoted as saying: "The utility men want news. That is propaganda, of course. That is what they are paying for and the only way to speed our propaganda is by means of speakers."